UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK
Case No. 08-13555 (JMP)
- -x
In the Matter of:

LEHMAN BROTHERS HOLDINGS INC., et al.,

Debtors.

- -x

U.S. Bankruptcy Court
One Bowling Green
New York, New York

October 7, 2010
9:06 AM

B E F O R E:
HON. JAMES M. PECK
U.S. BANKRUPTCY JUDGE

CONTINUED EVIDENTIARY HEARING re 60(b) Motions

Transcribed By: Ellen Kolman

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P R O C E E D I N G S

THE COURT: Be seated, please. Good morning.

MR. TAMBE: Good morning.

MR. HUME: Good morning, Your Honor.

MR. TAMBE: Jay Tambe for Jones Day for Lehman Brothers Holdings. May I approach?

THE COURT: Yes.

PAUL PFLEIDERER, WITNESS, PREV. SWORN

CROSS-EXAMINATION

BY MR. TAMBE:

Q Good morning, Professor Pfleiderer.

A Good morning.

Q Okay. Let's start where we finished yesterday.

At the end of the day yesterday, I believe Mr. Hume was asking you a question about BCI 292, and it was an e-mail exchange between Mr. Ricci and Mr. Clackson. Do you see that?

A Yes, I do.

Q And it has a subject line, scared to death. Do you see that?

A Yes.

Q And, in fact, Mr. Hume asked you, Professor Pfleiderer, do you believe that Barclays had good reason to be concerned about the risk that they had taken in acquiring all of these illiquid assets in the middle of the worst financial crisis since the Great Depression. Do you remember that question?

A I do.

Q And you generally agreed with that, that they had reason to be concerned, correct?

A I did, yes.

Q And similarly, Professor Pfleiderer, did Barclays have good reason to believe it had the deal of the century, as Patrick Clackson said in response?

A Perhaps they did, because this was a big deal. Obviously, it was something that was going to, if it worked out, allow them to achieve some strategic objectives, which I think was to establish a foothold or a presence in the North American market, which Barclays did not have.

Q And, in fact, that's the way it has turned out, correct?

A I would believe that they'd probably characterize it as that, but.

Q Let's some step back to some bigger things that you touched on yesterday. You spent a fair amount of time in your seven hours of direct, talking about the complexity of the instruments at issue in the transaction, right?

A I did, yes.

Q And your basic opinion as a financial economist is that these are very difficult to value in the best of times, and in September 2008, they were particularly difficult to value, correct?

A My opinion is that a good part of the assets that were

acquired were difficult to value, and they were particularly difficult at the time because of the market turmoil, or the market turmoil added to the difficulty.

Q And, in fact, I recall you saying you had a spectrum, the green to black spectrum, from level one to level three, and your view was, the level threes are certainly difficult to value, a lot of subjectivity, correct?

A That is correct, yes.

Q So are the levels two a little bit better, but still a lot of subjectivity, correct?

A Again, I would just qualify this by saying the marks that -- excuse me, the classifications that were used were Lehman classifications, and they weren't necessarily according to the difficulty that would be involved in those. But on a conceptual level, definitely as we move across that spectrum, things get more difficult to value.

Q Well, can we then agree whether it's Lehman classifying them or Barclays classifying them, there were level one, level two, and level three assets in the deal, correct?

A Yes, that's correct.

Q Okay. And using that as our base, level three assets you'd say require a lot of judgment, a lot of subjectivity to value, correct?

A That is generally correct, yes.

Q And you could reasonably expect a range of valuations to

come out of a level three valuation, correct?
A Because judgment is involved, that would generally be true, yes.
Q And that's your view with respect to level two, as well, it requires judgment, maybe perhaps not all the same degree of judgment and discretion, but some judgment and subjectivity with respect to level two assets, correct?
A There's judgment involving those as well, generally speaking.
Q And therefore, you could get a range of reasonable numbers, that's your opinion?
A That is my opinion, yes.
Q And, in fact, you would say even on level one, I think you said a few times yesterday, it's not all automatic. Even in level one, things that are classified as level one, may from time to time, have some small level of subjectivity, correct?
A In particular, the need to mark level one assets to an exit price involved some judgment. So even if we observed the actual transaction prices that are occurring in the market, there's still some judgment involved in determining how to mark those to an exit price. So even judgment is involved there, yes.
Q And so when you collect all of these ranges and judgments for level one, level two, and level three, you can, in your opinion, have a fairly significant range of possible valuations

LEHMAN BROTHERS HOLDINGS, INC., et al.

that come into play, correct?

A It could be significant, yes.

Q And in the time that was available the week of September the 15th through the closing day on September 22nd, your view is that no line-by-line CUSIP valuation could have been done with any great precision; is that right?

A I think that's definitely true, yes.

Q So if you're looking at this as a financial economist and trying to figure out the economics of the deal at the moment, not with the benefit of four, five, or six months of due diligence, but at the moment, if you want to fairly describe the economics of the transaction, you ought to be describing this range of uncertainty and range of reasonableness, correct?

A I assume that the question is how the question is asked of what you're actually getting, and the best way I think to describe it, is to give some sort of notion as to what the value might be, and then to indicate that there's great uncertainty about that.

Q Right. And, in fact, I mean, we spent a good part of yesterday talking about the types of uncertainties that surround these assets, correct?

A Yes, we did, in particular, for example, with Pine.

Q Yeah, hours of testimony, detailed testimony, asset class by asset class, as to the range of values and the range of considerations, some of them very subjective, that could come

into play, correct?
A Yes, that was correct.
Q Okay. And so if you are in the midst of that week of September 15th, and you're talking about the transaction, and you as a financial economist were listening to this, you'd want to know, you know, what are these uncertainties, what is the range of reasonableness so I can make an informed decision about the economics of the transaction, wouldn't you, sir?
A You know, as I said, I think the characterization that would probably be most appropriate is to give some notion of what the level of valuation is, and then to indicate that there's a tremendous amount of uncertainty around that, and that the person that's acquiring the portfolio is because of that, taking some risk, but give a notion as to what the value is, and what the range of uncertainty is, in the sense of just saying that there's a fairly large amount of uncertainty.
Q Now --
A I think it's difficult to quantify. So if you're looking at a question, could one put a confidence interval and say with 90 percent of confidence it'll be between X and Y, I don't even think that was possible at this time.
Q You had a discussion I think with Mr. Hume about some of the -- I think you referred to them as publicly available information or public disclosures that were made during the week. And, in particular, I think he drew your attention to

the analyst call that was hosted by senior management of Barclays. Do you remember that?

A I do.

Q Okay.

MR. TAMBE: So if we could pull that up. And I believe that is BCI Exhibit 110.

Q And it ought to be in the binder that was given to you, but we could read it on the screen. It may be faster.

And in particular, I want to draw your attention to the third paragraph on page two.

MR. TAMBE: And if you could blow that up, please.

Q Now, this is a description by senior management by Mr. Varley, right, Group Chairman of Barclays describing this transaction to analysts. And that second -- the third sentence he states, we are acquiring trading assets with a current estimated value of seventy-two billion dollars, and trading liabilities with a current estimated value of sixty-eight billion dollars, for a cash consideration of 250 million dollars.

Do you see that?

A I do, yes.

Q And you have reviewed this analyst transcript before, correct?

A I've read this, yes.

Q And you see no extended discussion in this transcript

about the great, tremendous amount of uncertainty about these assets, and about the large number of level two and level three assets, and all of the subjectivity involved in coming up with values. There's no such discussion in this analyst call, is there, sir?
A Certainly not in this paragraph, no.
Q Okay. Well, you have reviewed the transcript, correct?
A Yes.
Q All right. And you haven't located any other spot in this transcript where there's an extended discussion about the tremendous amount of uncertainty, as you phrase it, about the valuation of these assets, was there, sir?
A I'd probably want to go back and refresh my memory by reading the entire transcript, but I don't remember any particular discussion, for example, of level one, level two, or level three in this conference call.
Q Nor do you recall any specific discussion of a tremendous amount of uncertainty with respect to the valuation of the assets, correct?
A Again, I'd want to go back and read it carefully, but sitting here now, I don't remember those words being used, but they may have been at some point in the question and answers that followed, just not sure.
Q There was discussion about steps taken to de-risk or mitigate the risks of the transaction. Do you remember that

being a topic discussed in the analyst call?
A Yes, I do.
Q Okay. So if we'd go to page three and at the bottom of page three, and you may want to --
MR. TAMBE: If you can pull that up. And actually, the question that is a few lines above that from Mike. Right there.
Q The question from Mike, yes, the second question was just trying to get a sense of good assets, bad assets, and impairments that have -- that would've already been taken either through the P&L or to AFS, on the assets that you are acquiring.
And the answer is given by Chris, and you see -- you know that that's a reference to the Group CFO, Chris Lucas, correct?
A Uh-huh, yes.
Q See a guy at the bank.
A Yes, I would believe so, yes.
Q And what he says is, he's talking about a seventy-two billion dollar number, and he says, I would say I have a total -- out of the total of 72.7, which is a net number, the vast majority of those assets are quoted equity government and agency paper.
Do you see that?
A Yes, I do.
Q And he wasn't incorrect in describing it in those terms,

correct?

A Well, I -- actually, when you look at what was acquired, vast majority, may be a little bit too strong a statement, because many of the assets again, speaking about what we looked at yesterday were at level two and level three, the vast majority of -- I shouldn't say the vast majority, but the majority were level two and level three.

Q And then he goes on to say, there's a small amount of mortgage paper, which has been heavily written down and included in those numbers.

Do you see that?

A Yes, I do.

Q So you see there a reference to the writing down of values on certain assets that were being acquired, correct?

A In terms of the mortgages, yes.

Q Okay. And then he goes on to say, so we've been through a process where we took the original marks, reviewed them, and then took some further write-downs, but that is against a very small portion, less than five percent of that book.

Do you see that?

A I believe the mortgages would probably be less than five percent. I'd have to go back and calculate, and it would depend upon whether you start with it before the write-down or after the write-down in calculating that percentage. So I'd have to go back and make sure that that calculation was done

correctly.

Q Right. But you and I can agree that certainly there's nothing in that answer from Mr. Lucas that says, we're at a 72.7, but it could be plus or minus five billion dollars because of the tremendous amount of uncertainty?

A It's clearly not stated in that way.

Q Okay. Let's go to page four, in the first paragraph on page four to see how the description of the transaction continues.

And that same question is thrown over to Bob, anything further you want to add, Bob, and that's a reference to Bob Diamond, correct, President of Barclays Capital?

A I believe so, yes.

MR. TAMBE: And if you could go to the -- start highlighting at the word first and foremost, all the way down to the end.

Q And what Mr. Diamond says is, first and foremost, as Chris said, we've got to choose which inventory came with the deal, and primarily we chose things that were important to the underlying businesses, he says. So for example, many of the positions we took in equities had to do with our cash equities business. I think the second thing that was important is we had just completed seventy-two hours of due diligence on every position, so when it came time to make the decision on what came, we personally had been doing due diligence and were able

to establish the marks.
     Do you see that?
A   Yes, I do.
Q   And you don't think Mr. Diamond was making that up when he said that on the analyst call, was he?
A   I certainly don't think he was making it up. I don't know what he means by established the marks, and I don't know whether when he said that he was doing it on every CUSIP that he actually meant that it was on a CUSIP by CUSIP basis, as opposed to breaking the portfolio down and analyzing it more in classes that would cover every CUSIP, so.
Q   He certainly didn't give that explanation or qualification to his answer saying, well, we did this, but we didn't do this on a CUSIP by CUSIP level, we did this on an asset.
     None of those qualifications were in his answer, correct?
A   No, there's no clarification of that sort, but I am wondering how in seventy-two hours you could've analyzed 12,000 CUSIPs, and so I'm trying to reconcile what he might have meant by saying what he's saying here, with what I think is almost a physical impossibility of doing a CUSIP by CUSIP analysis on so many assets.
Q   Okay. And you see no disclaimers in Mr. Diamond's answer about well, we did all of this, and we did this due diligence, but at the end of it, there may be a swing of plus or minus five billion dollars, because of the tremendous amount of

uncertainty?
A No, he's not saying that here.
Q Now, let's go to page 13, and towards the bottom of that page, it's the answer from Chris Lucas.
MR. TAMBE: In fact, let's start with the second sentence, start highlighting it.
Q And with reference to mortgage assets, he says, those are marked down and then marked again through the due diligence process.
Do you see that?
A Yes, I do.
Q And he says, so I think to do any direct comparisons are actually very difficult for the reasons we have said before, and the fact that the vast majority of the book is very high quality, easily tradable assets and liabilities.
Do you see that?
A Yes, I do.
Q Okay. So here you see no description of the tremendous amount of uncertainty about values that you described in your testimony yesterday, correct?
A No, I do not.
Q Now, this was not the only set of disclosures being made, correct? There were disclosures being made to this Court about values in the transaction, right?
A Yes, I believe so.

Q And then the Court was being asked to weigh some economic values in terms of the benefit to the estate, right?

A I believe that was the situation, yes, indeed.

Q And one of the documents through which the Court was first apprised of some of the values was the asset purchase agreement, which was submitted with the motion seeking the establishment of processes for the sale, correct?

A I believe so, yes.

Q Right. And that's the -- you're familiar with the asset purchase agreement, correct?

A I am, yes.

Q And that's the document that has the approximately seventy billion dollars of long positions, approximately sixty-nine billion dollars of short positions, correct?

A That's correct.

Q And we can go to the document, but you didn't see any discussion in that document, other than the use of the word approximately off, there was a tremendous amount of uncertainty about the seventy billion, it could be seventy-five, it could be sixty-five, it could be fifty, there were no such disclaimers about those valuations in that document, correct?

A I don't believe so, no.

Q And in addition to documents that were submitted to the Court there were hearings held, correct?

A Yes, that is correct.

Q And in particular, there was a hearing held on the evening of Friday, the 19th, right?
A Yes, I believe that was -- and I think it even spilled over into Saturday.
Q The early hours of Saturday morning. And that was the hearing at which the Court was asked to approve the transaction, correct?
A I believe that's correct, yes.
Q And there were some representations made to the Court at that time about the value of the trading assets, correct?
A Yes.
Q And you recall Ms. Fife saying at that hearing --you've read the transcript, correct?
A Yes, I did.
Q Okay. And she describes the transactions, we're only selling assets that have a value of 47.4 billion dollars. Do you remember that?
A That's my recollection, yes, of what I read.
Q Okay. And in that description, you had not seen Ms. Fife or anyone else in the courtroom stand up and say, well, wait a second, those are a lot of level two and level three assets in there, there's a tremendous amount of uncertainty, it could be 47.4, it could be fifty-five, it could be forty, there's a big zone of uncertainty, Judge, you should know that, because you may want to take that into account in deciding the financial

economics of this transaction?
A Well, I have two observations. First of all, I think what you did is give a point estimate, and as I sit here and reflect on what you're saying, and think about my economic opinions, basically what's being represented here, if you just read this in both the conference call here and in court, if there's no mention of the uncertainty, which I do believe from what I have analyzed was there, then basically, outside bidders should've been much more inclined to bid, if they didn't think there was much uncertainty there.
So I think that actually reinforces my economic opinion that even if the deal is characterized as not having a lot of risk, which I think it did, the fact that no bidders came to -- alternative bidders came to bid on it, either indicates that they didn't want to take this transaction even with a little bit of risk, or they realized that there was a lot of risk there. So --
Q We'll come back, sir, to what other bidders may have thought. I was actually focused on what representations were made to the Court, what the Court thought about what transaction it was being asked to approve.
A In that case, I think all that was given was a point estimate.
Q Now, in all the documents and transcripts you reviewed, you haven't seen any discussion where the lawyers, Ms. Fife,

Mr. Miller, who was speaking in court were advised, there's a great deal of uncertainty, a tremendous amount of uncertainty for the valuation of these assets. In fact, there could be swings of five billion dollars each way in the valuation, before you make any representations to the Court, be aware of the following facts.

Did you see any documents like that, sir?

A Well, I think that one thing that I did, and I'd have to recall precisely how it was said, but I think when Ms. Fife was speaking, she was saying that because of tremendous uncertainty and a lot of tumultuous outcome over the week, the deal had changed substantially from what it was on Tuesday to what she was reporting.

So that in itself, I think, would indicate that there was a fair amount of uncertainty. But again, it wasn't qualified or quantified, I should say, by giving a range of values, at the 90 percent confidence level, but I think in the context, and I've have to go back and read exactly what she said, or perhaps it was Harvey Miller. There was some language, I believe, indicating how much had changed and basically that there was a lot of variability that was occurring over the few days.

Part of it in terms of presumably what assets were available, but also in terms of potentially what they were valued at.

Q Well, why don't we just look at what she said, because you seem to have some uncertainty as to what she may have said, and how she may have qualified the 47.4 billion dollar number.

MR. TAMBE: M-261, please. That's the 9/19 hearing transcript at pages 46 to 47. I believe it begins at the bottom of 46 on to 47.

Q That's the entirety of her description on the 47.4, and what she says is that changes in the market, from the time the transaction was actually entered into till now, the markets dropped, and the value of the securities dropped as well.

So originally, we were selling assets that had a value of seventy, approximately seventy billion, and today, Your Honor, we're selling -- only selling assets that have a value of 47.4 billion dollars, correct?

A Yes. It --

Q It didn't say, they have a value of 47.4 billion dollars, plus or minus 5 billion even today?

A No, this is precisely what I was remembering. I think I actually remembered it rather well here. What she was saying was that the value in just a few days had changed substantially from seventy to 47.4, and if anything, indicates a fairly large amount of uncertainty and risk, I would think it would be that.

So again, she didn't quantify -- excuse me, quantified around a point estimate, but one would read this and certainly come to the conclusion that because of market conditions,

there's a fair amount of uncertainty here.
Q So someone reading this, in your view, could have come away with the conclusion that, it could be 47.4, or it could still be seventy billion, or it could be thirty billion. Is that what you thought she was conveying by using --
A No, I don't think that's what she was conveying at all. I think what she did convey here is very simple. A few days ago, it was seventy billion, markets have changed, and now it's 47.4. That's a fairly big delta in just a few days. I think some of that, of course, is due to some assets not being available, but it was also market value changes, and I think in this context, it certainly indicates there's a large amount of uncertainty.
Again, she's given a point estimate here without a ninety percent confidence in her -- some confidence and her go around it, but the context is one certainly that gives a notion of great uncertainty.
Q And, in fact, you made a very good point. The point is, the difference from seventy billion down to 47.4, you know it wasn't simply because of market movements, right? There were assets that were no longer available.
A That's right. I said --
Q It was substantial. There were tens of billions of dollars of assets that were no longer available. It wasn't market forces driving down the value, it was the lack of

availability of assets that was responsible for a lot of that movement, correct?

A It was both. I believe that that's what she's indicating here.

Q Now, in any of the court records that you reviewed, did you find prior to the Court being asked to approve the transaction, any discussion, broad disclaimer that the numbers that are in the APA, the numbers that have been offered, the hearing, that these are subject to a tremendous amount of uncertainty, large swings in value, the deal could be worth five billion more for Barclays or five billion less for Barclays, anything like that?

A I'd have to go back and review it all, to say anything with complete confidence. In sitting here right now, I don't remember a specific discussion that began to quantify a confidence interval or give a risk range of this work that you just said. But there may be, I just don't remember, sitting here today.

Q And to the contrary, I think one of the descriptions or one of the pieces of evidence that was offered to the Court, was a suggestion that there had been a line by line valuation done, correct?

A You'd have to point me to that. I don't recall that right now. It may --

MR. TAMBE: Will you go back to the transcript,

please, the 9/19 transcript at page 109, line 5? It's 109, line 5. Yeah.

Q And this is Mr. McDade's Q and A.

On the absence of a closing balance sheet having been prepared, can you prepare -- can you please describe for the Court how it is that the debtor determined that fair value was being realized for the sale of these assets? For the assets? Yes. The individual assets in the balance sheet, the trading inventory was bottom-up, meaning individual line item detail processed through all of our individual risk business units in coordination with the normal finance professionals who are incorporated in the valuation process.

Do you see that?

A Yes, I do.

Q Had you considered that testimony as part of rendering your opinion, sir?

A Well, the context that I would consider that in, is how the APA value of seventy billion was calculated, which seems to come from the books. So I'm not sure whether that was from the books of GFS, for example, with the notion that what was carried on the books was subject to the process that he's talking about, or whether he's talking about corrections to values that were in GFS.

Q Well --

A So I don't know how to interpret it.

Q You're not interpreting.
A That's correct.
Q Mr. McDade obviously knew what he was talking about, he swore under oath as to what he was talking about, correct?
A He was talking about some process. What I don't know, sitting here, is whether that was a process that basically was filtering through GFS, which is from what I can see, presumably the source for the seventy billion that was in the APA, or whether there was some other process that went beyond the GFS book value. That I don't know.
Q Going back to the 47.4 that you described by Ms. Fife as a point estimate.
Do you know one way or the other, sir, whether the number that Ms. Fife gave the Court included any liquidation values in it?
A No, I do not.
Q And the fact of the matter is, as you sit here, you have no idea where the 47.4 number comes from, correct?
A No. Because in her testimony, she didn't, at least I didn't see it, a description of how she'd calculated that, no.
Q Let's switch gears to a topic you spent some time talking about yesterday morning, which was the five billion dollar discount at inception, the GFS process that you took the Court through.
MR. TAMBE: And if you could start perhaps in the

Barclay demonstratives, if we could pull those up, and we could start with slide 11, please.

Q That's a slide you prepared, correct?

A That is correct, yes.

MR. TAMBE: Steve, is it possible to just enlarge it slightly?

Q If you don't mind losing the heading, we'll focus on numbers.

A Sure.

Q And just so I understand what you have here, is you have a series of numbers at the bottom, which you have drawn from your analysis of the GFS data, correct?

A That is correct.

Q Right. And that's the GFS data as of each of those dates at the top of the column, correct?

A That is calculated based upon the GFS data that was available for each of those dates.

Q And you make two adjustments at the bottom, and I guess you're doing it to make sure you're comparing apples to apples.

A That is correct. I'm subtracting off the mortgages, which were not included in the long positions in the APA, and then adding in the short-term agreements, collateralized short-term agreements, which were.

Q And so by making those adjustments, now you're comparing apples to apples across the GFS system, and you come up with a

series of numbers, the highest of which is 65.8, correct?
A That is correct, yes.
Q And on slide 12 --
MR. TAMBE: Again, if we could focus on the numbers, please.
Q -- you take the last three columns or three of those numbers from the previous slide, correct, the 65.8, the 64.4, and 62.57, correct?
A That is correct.
Q Right. And your view was when properly normalized, that's what GFS shows the value of the long position to be as of each of those dates, correct?
A If you mean properly normalized to mean subtracting off the mortgages and include --
Q That's exactly what I mean.
A Very good, yes.
Q The process that you suggest. And then on the left side, what you're comparing it to, I guess, are three other spreadsheets, correct? For example, you've compared to the Steve Berkenfeld schedule, which has also been similarly normalized, my word, right?
A If I could interject, I don't necessarily characterize those as spreadsheets. It may have been in the form of a spreadsheet, but I've never seen the spreadsheet. I've just seen a hard copy, photocopy, if you will, of that schedule that

Mr. Berkenfeld signed. It may have been in spreadsheet form, but it may not have been.

Q That's right. I mean M-2, the Berkenfeld schedule with his initials on top, that's a document that you have never seen any spreadsheet back-up for, correct?

A I don't believe I have, no.

Q Okay. So just working off of that one-page document, again, you made those adjustments, minus 2.7 plus 10, again, you're comparing apples to apples, correct?

A Well, I'm basically taking the data from GFS on the right-hand side, and comparing it, according to the classifications that were on the Berkenfeld documents. So in that sense, it's an apples to apples comparison.

Q All right. And one of the reasons why you made those adjustments to the Berkenfeld schedule is to compare it to the seventy billion dollar long position described in the APA, correct?

A The subtraction, for example, the 2.7 and the addition again in the ten, yes.

Q Right. And in your view, your opinion is, that that gets very close to the seventy billion dollar number that's in the APA, correct?

A 69.3 is relatively close to seventy, yes.

Q Okay. And you conclude from this analysis that reviewing the GFS data doesn't show any mark down off the Lehman's values

to arrive at the seventy billion dollar number, correct, because all these values are less than seventy billion dollars?

A That is correct.

Q When you finished this analysis, did you stop and ask yourself a question?

A Just --

Q Did you ask yourself, why none of this adds up to seventy, why does the GFS data in the 9/12 column, the 9/15 column, the 9/16 column fall short of seventy billion dollars, by close to five billion dollars, more than five billion dollars as you go on, not close to seventy?

A That's correct.

Q Did that cross your mind, sir?

A It did indeed.

Q And what's your answer?

A That the values that are on the APA are above what was in GFS.

Q Well, values in the APA are greater than GFS. To do that, you'd have to mark up the assets on Lehman's books, to go from Lehman's valuations to the values that appear on the APA, right?

A Well, again, in the APA what it said was approximately seventy billion. And again, I'm not a lawyer or an attorney, so I don't know how these contracts are drawn up, but I would interpret it as a layperson to be giving a value, a notional

value almost of -- I shouldn't use notional because that has other meanings, but a value that gives some notion of what the scale is.

The question that I addressed here was a simple question, and the question is, is that a markdown of five billion dollars or more from what was on the books, and when one goes back and looks at the books, one finds that it's not.

Q Well, you suggested that maybe what's happening here, is that the assets are being written up to be included in the APA description, right? That's one way you can get to seventy when the GFS data gets you only to 65.8, correct?

A Well, I don't know if I'd use the term written up. I think the contract simply gave a value, and the question that I addressed is whether that value was understated.

Q Well, it did more than just give a value, right? It used the phrase book value in connection with the seventy billion.

A Correct.

Q That didn't say, we just picked a number out of thin air, it said seventy billion dollars book value, right? So the impression was that that seventy billion dollars came from Lehman's books. There's an alternate explanation, correct, sir, for the disconnect here?

A I --

Q Right?

A I basically did an exercise of simply looking at what was

in GFS books and comparing it with what was in the APA.
Q No, I know what you --
A But I didn't try to come up with an explanation other than to ask the question, the very simple question is whether the APA understated what was on Lehman's books, which it did not.
Q And then you answer that question --
A Right.
Q -- but the analysis you did actually raises another question, which is, why is this falling five billion dollars short? If it's coming from Lehman's books, why is it off by five billion? Are there assets that are not captured by GFS, sir, is that what's going on?
A Again, if we look at what Barclays actually got, we see that very little of it was not in GFS, and I talked about the matching. So I assume certainly there are assets in GFS that are not part of LBI, but the filter that's used is to look at the assets that are in LBI.
Q Well, one thing we can rule out, right, is there's been no testimony, no evidence, that people from Barclays and Lehman's sat around conference room tables saying, oh, Lehman, you've got that marked too low, let's mark it up. That didn't happen, no evidence of that, right?
A I don't believe so.
Q In fact, all the evidence that has come in, in forms of testimony, when people have talked about the Monday and the

Tuesday, has been about marking down the values that appeared on Lehman's books, correct? Lots of testimony about that, correct?

A I believe that those words were used, and of course, we see that the marks on the books are declining over time. Again, to reflect changes, as we talked about before, in market values potentially as well as the assets that are there.

Q I'm not talking about declining in values because of the passage of time. What Mr. Varley talked about and what senior management of Barclays talked about in that analyst call, we've marked down assets.

A But you have to be very careful there. The assets that were marked down that were mentioned in that conference call were the mortgages, and the mortgages are being taken out of this calculation.

Q But still no explanation of a marking up process that would've increased the values from the GFS values to the seventy billion?

A I don't believe I've seen any testimony to that effect, no.

Q Now, you analyzed a couple of other documents in connection with your work.

MR. TAMBE: Let's take a look at M-264, please. And can you just blow that up?

Q Are you familiar with this e-mail, and there's a

collection of spreadsheets that appear behind it?

A Yes, I believe so.

MR. TAMBE: And if you could just scroll through those spreadsheets to the last one. If you can increase that.

Q You see here a spreadsheet that has different values on it than in M-2 of the Steve Berkenfeld document, although the layout and format is similar to the Berkenfeld document. Do you see that?

A It certainly has a similar form to the Berkenfeld document, at least the assets that are here on the left-hand side, I believe.

Q And this document has seventy-seven billion dollars in total assets on the left-hand side, eighty-one billion dollars of total liabilities on the right-hand side. And you have, in the course of your work, looked at some handwritten notations that were made on various versions of these types of documents, correct?

A I have looked at those, yes.

Q And I think you talked about one of them yesterday, if we can go back to the Barclays' slide, slide 9, which is BCI 1103 is the exhibit number.

And you did some analysis of what was appearing on those handwritten notations.

MR. TAMBE: If you could just increase the size of those handwritten notations. In fact, why don't you pull up

Movant’s Exhibit 15, because that’s what that document is.
Q And you did some analysis of those handwritten notations to try and reconcile these numbers that are in excess of 70 billion dollars with the analysis that you had done, the GFS analysis that you had done, correct?
A Well, the 77.4 you need to subtract again the mortgages to 6.5, and as I explained yesterday, you also need to subtract 2.3, which relates to those entries for other assets and investment in consolidated subs, and you need to subtract the goodwill and you get less than seventy.
Q Okay. And so you did that analysis on that document. None of the slides you presented yesterday provided any analysis of what was going on on the liabilities side of this, correct?
A No. Because I was focused on the APA and the seventy billion in long asset calculation.
Q And at least conceivably one of the ways that there could be losses after Lehman’s marks is either by writing down the value of long positions, or writing up the value of short positions, correct?
A Can you restate the question, please?
Q When you think about the concept lost to our marks, that’s a phrase you’ve seen, a common one?
A Yes.
Q A loss to our marks, of Lehman's marks, can come about in

two ways. You take the long positions and value them down, or you take short positions, and you mark them up.

A That would also -- well, I would be careful about saying lost to marks. I need to understand what the process is by which you're writing these up or writing down. If what you're doing is basically updating those to get better marks, than I don't know that I'd characterize it as a loss to marks.

But certainly if the liabilities go up, the net value is going to go down.

Q And no part of your analysis looked to see what kinds of changes were being made on the GFS data, which also carry short positions on the valuation of the short positions?

A No, that's correct.

Q I believe one of the conclusions you have drawn from your analysis of various spreadsheets and GFS data is that at no time during the week of the 15th did you see any GFS data or spreadsheets that put the value of Lehman's long positions over seventy billion dollars, correct?

A That is correct.

MR. TAMBE: If we could pull up Movant's Trial Exhibit 190, please. And if we could just enlarge the e-mail chain.

Q Is this an e-mail chain that you've seen before?

A I believe so.

Q You have?

A I believe so. I may need to -- I remember when -- from

LEHMAN BROTHERS HOLDINGS, INC., et al.

James Hassler (ph), I'm not sure how you pronounce his name. I believe I've seen this, yes.

Q Okay. And there's a spreadsheet attached to this, correct?

A If it's the one I'm thinking of, I believe, yes.

Q And there's a reference to market data and GFS data in this document, correct?

A Yes.

Q Okay. And it says, Bill's going to retrieve the GFS market values for the list. Do you see that in the middle of that e-mail chain?

A Yes, I do.

Q Right. And then Bill Parrinello responds, here's the file, found a price for all CUSIPs. Do you see that?

A Yes.

Q And then at the top of the e-mail, it says with marks in -- within quotes, K. Do you see that?

A Yes.

Q Okay.

MR. TAMBE: And let's go to the spreadsheet if we can. I think we have it in native format, correct?

UNIDENTIFIED SPEAKER: Excuse me. I am just wondering, is this in the binder here?

MR. TAMBE: I'm not sure if it's in the binder. I don't have a tab number. It's a previously marked exhibit. If

it's not, we can get you a copy. We're going to look at the spreadsheet, so I'm not sure if you want to look at --

UNIDENTIFIED SPEAKER: I just would've liked to have seen the whole e-mail.

MR. TAMBE: Oh, sure.

UNIDENTIFIED SPEAKER: If you could get it to us, that'd be good.

BY MR. TAMBE:

Q When you reviewed this document, Movant's Exhibit 190, and the spreadsheet that was attached to it, did you pull up the spreadsheet and see what the values were in this spreadsheet?

A I don't recall personally doing that. Staff may have done that. My analysis was based upon going to GFS and pulling down the actual data from GFS.

Q And if you'd roll over to column K on this spreadsheet, you'll see that's the column that was referenced in the e-mail, column K says market value.

A Yes.

Q Did you ever sum up the amount that appears in the market value column of this spreadsheet?

A Again, I personally did not.

Q Would it surprise you that it's in excess of seventy billion dollars, approximately seventy-three billion dollars?

A Well, again, does this include the mortgages?

Q You saw the spreadsheet before. Do you know?

A I saw the spreadsheet, I didn't look to see if it included mortgages. If it includes mortgages, one has to subtract off the mortgages, one has to subtract any other assets that were not part of the loan inventory, so in fact, it wouldn't surprise me at all, because we saw that there are certainly situations, we just looked at one, where the value is seventy-seven, but once you make the adjustments to compare apples to apples instead of apples to oranges then it's under seventy.

So what this may be is an orange, and it has to be converted into an apple before you can actually compare it with the 70.

Q Okay. But you don't know as you sit here, whether that exercise was ever done by you or your staff, with respect to this spreadsheet which purports to be based on GFS data?

A All I can say sitting here, is that I did not personally do it.

Q Now, we'd spoken a little bit earlier about adjustments to marks or marking assets to value, to market values, correct, in the context of the analyst call?

A In terms of the adjustment to the mortgages, I believe that's --

Q Yes.

A -- what you were referring to, yes.

Q And you are familiar with testimony that's been given in this case by Mr. Varley and others about the concern that

Barclays had for a buffer and for appropriate valuation of the assets, correct?
A Yes. Certainly the discussion about the buffer and the importance of maintaining the buffer is an important consideration for Barclays.
MR. TAMBE: If we can pull up the Barley trial transcript of June 22nd, 2010, and starting with his answer, line 5, of page 102. Just scroll over to the next page and let's read this page, and then we'll move over.
Q Mr. Barley was testifying about negative goodwill and the buffer in general, and he starts by saying, and, at line 8, if I then think about the transaction that was announced, and I know we're going to come to it in due course, on the transaction that was announced on the following date, when of course, we were armed with more contemporary information, because it was the nature of the transaction that was being announced the following day, there was indeed a mismatch or buffer between the number of assets and the number of liabilities.
Do you see that?
A Yes.
Q And he goes on to describe the buffer, correct? And let's go to page 103. And the question and answer, starting on line 2 down to line 17.
And one of the way you accomplish that, putting a

condition precedent on it, was to insist that there be a discount to the asset valuation, as to the assets that Barclay was taking on in Lehman 2; is that right?

See that question?

A Yes, I do.

Q And you understand Lehman 2 to be a reference to a deal that was announced and that was the subject of a sale order motion, correct?

A I understand that to be the sale of LBI instead of LBHI, yes.

Q And his answer is, he doesn't quite like the word discount, but he answers it as follows, no, it's not how I think of it. I tried to be precise in answering your question earlier, because I do think of -- I see differently the assessment of realistic valuation through the mark to market, and then a buffer between assets and liabilities.

Do you see that?

A I do.

Q Okay. And do you understand that Mr. Barley was describing two scenarios. One is, you first mark the assets to what he would believe the appropriate value, and then you ensure there's a buffer between those assets as valued, and the liabilities, correct?

A I believe that's what he's saying here, but I would qualify that, I'd like to go back before I say anything

definitively to read it in the broader context and make sure that I'm properly interpreting what he's saying. But I believe that's what he is saying.

Q And, in fact, if you go on in his answer, I think he turns back to that issue, I would actually, just as a term of art, as opposed to a term of science, describe the realistic valuation as the mark to market. That's what we were seeking to do. Then having established a mark to market valuation of assets, we were then seeking to ensure that there was a buffer between assets and liabilities to create a positive capital outcome, not a discount, I don't see it as a discount, I see it as a buffer.

Do you see that?

A I do.

Q And again, a discussion of these dual processes, one is the mark to market, and then ensuring there's a buffer between the properly marked assets and liabilities, correct?

A Again, just reading this page that would be my interpretation of what he's saying.

Q And it was your understanding in terms of what people were doing in those first couple of weeks -- first couple of days of that week, the Monday and the Tuesday of the week of the 15th, is trying to come up with realistic values for the assets that were being acquired, and then making sure that there was some kind of a buffer between the financial assets being acquired

and the liabilities being acquired, correct?
A I don't know that that is a proper characterization of all the activities that were being done. But I think that overall, there was a concern, first of all that the assets that they were getting, if they used the Lehman marks, were over valued relative to what they were actually worth. And then there is the very legitimate concern, and I spoke about this yesterday, that you're acquiring a large portfolio, and you're putting yourself in a position of risk, and that buffer is basically to offer some protection, given the risk that you're taking on.
Q And the process that was described of establishing values, that was not a process to mark up values, it was to mark down values, correct? The concern was that Lehman's valuations were overly optimistic?
A Well, I wouldn't characterize it quite that way. I would characterize it as a process to mark the values that were on Lehman's books to the values that were reflected in the market. So that's not a process of either marking it up or down, it's a process of marking them to what they are in the market.
It turns out that over this week, market values were declining, so the process of marking it to market would mean generally speaking, that you'd be marking them down. But I would distinguish going in and saying we're going to look at the marks that are on the books, and look at where the market is, and adjust the marks to where the market is, as opposed to

just simply going in and saying, we're going to look at the marks on the books and mark them down, without looking at what the market is doing.

So I would characterize it in the way that I did, and not simply saying that they were marking them down.

Q Okay. And this process of marking was a process -- it wasn't just Lehman doing it by itself, it was Lehman doing it across the table from Barclays, correct?

A Again, all I have to go on here is the testimony that I read in some depositions. I wasn't there at the time, so I don't know exactly how the bargaining, if you will, or the process of negotiating this deal was done.

Q And you certainly defer to the people who were actually at the table negotiating the deal, to describe the mechanics of what it is that they were doing, correct?

A I wasn't there, they were, so they have a distinct advantage over me, I would say that.

Q And we could take a look at the trial transcript of Mr. Lowett. Mr. Lowett testified about that process sitting in the very chair that you're sitting in. You read his testimony, correct?

A I believe I did, yes.

Q And it was the April 29th transcript of Ian Lowett's testimony on page 92, line 19.

And, in fact, Mr. Lowett was describing what was a process

to get at a number that Barclays was willing to pay, a negotiated figure. The question he's asked is, now you agree, sir, that the difference between the amount reflected on Lehman's books and the amount that Barclays would pay was a negotiated figure, correct.

Answer, well, I don't know if it was. If it was, it was a number that emerged as a result of the activities of the various traders determining what value was aggregated together. And then that was, again my understanding, approved by the negotiators of the trade.

Over on the next page.

Okay. And in the end, it was what was agreed to between the parties in their negotiation sessions, correct? Again, I wasn't a party to those negotiation sessions, so I don't know what that was, but certainly my understanding was that the traders were meeting with their counter parties and agreeing what was the appropriate value for those securities, given the nature of the environment, and the market that we're dealing with.

MR. TAMBE: And if you'd continue at the next Q and A.

Q And you understood the difference was in the range of five billion dollars between the amount shown on the books and the agreed price, correct.

Answer, I understood that there was a difference between what was on our books, and what was the outcome of that

process, yes, and that was -- my understanding was that there was around five billion dollars, but I didn't know that, but I understood that.

Do you see that?

A Yes, I do.

Q And you have no reason to believe that Mr. Lowett wasn't accurately describing his understanding of the negotiations process?

A Well, I would just make two observations. First of all, he's in somewhat of a similar position to me because he said that he wasn't there observing it. But secondly what he described was basically a process of, as I read his testimony here, of doing exactly what I said, which is taking the marks and marking them to where the market is.

So that was exactly what I thought that would be the notion of the appropriate thing to do. If the marks are stale, you're marking at an asset at a hundred, and the market has moved, and it's now ninety, then using that hundred is misleading when the market price is ninety.

So he mentioned about traders adjusting prices to reflect where the market is, that was in sum and substance what I think he was saying.

Q And in all your years, have you ever heard of a broker-dealer marking its own assets and its own books in negotiations with a counter party, sir?

A Well, in a sense that's exactly what is done, because when they're marking their books, they're marking it to transactions that are occurring in the market that they themselves may have made, so when you buy an asset -- when a broker-dealer buys an asset, there's a negotiation oftentimes that will happen in that transaction between the broker-dealers, the buyer, and someone who's a seller. And that could be a negotiated deal. And then when the asset comes on the books, it comes on the books at whatever that negotiated price was.

So this is different because obviously it's not a run of the day occurrence that you're in a situation like this, when you're marking a portfolio. But when you look at it on the micro level, that actually does occur.

Q Yeah. Well, this wasn't on a micro level, this was on a macro level, fifty billion dollars' worth of --

A That's right. But I'm saying that the macro level has the same sort of characteristics of what happens on the micro level.

Q Let's turn to a different topic. Let's turn to the issue of the JPM inventory. You were asked about Professor Zchemiasky's (ph) valuation of the JPM inventory yesterday. Do you remember that?

A Yes, I do.

Q Okay. And just to make sure we're all on the same page, I'm going to just have the rough transcript pulled up from

yesterday. I'm going to ask you some questions about the answer you gave.

A Sure.

MR. TAMBE: It's page 8648 off the rough, please. And it's towards the bottom, line 17. 8648. 8648.

(Pause)

Q All right. Starting on line 17, you were asked --

MR. TAMBE: If we could just increase the size of that, please?

Q -- and what is your understanding of Professor Zchemiasky's valuation difference with respect to those securities, the JPM securities, and does it make sense to you as a financial economist.

And you say, my understanding is that he, and I believe other movants as well, but he's asserting they should be valued as of the 19th of September, several months before. And usually I don't state things as strongly as I'm -- next page -- going to state this, but I have to confess makes absolutely no sense to me as an economist whatsoever, and gives rise to all kinds of really perverse outcomes that make no economic sense to me.

Do you see that?

A I do, yes.

Q Okay. And if we can go on and read the rest of the answer, you go on to explain, I guess, why you feel so strongly

about it.
A Uh-huh.
Q So that's a rather strongly worded statement, but I just can't make sense of that as an economist. But that would make sense as a way to value a claim that was delivered at a point because it was then -- it makes a great deal of difference as to what was delivered at the time Barclays -- if you do that type of accounting, would've taken, say, two million dollars in security's worth on December 22 if those two million had been worth 14 million in September, because then it would've had a bigger, bigger gain, and of course, that's absurd, because it's not going to take two million when it can take five million.
And so you come up with all kinds of absurd, absurd results with the type of calculation on that basis, so it doesn't make any sense to me as an economist. In fact, I would, just to maybe strengthen my statement --
MR. TAMBE: And scroll down, Steve, to the next page.
Q I would love to live in a world where you could do that type of trading, because that would almost create an arbitrage like machine. It doesn't make any sense.
Does it make any sense to think about this transaction, the settlement that was approved by the Court as 1.5 billion dollars in cash consideration, along with the securities that were going to be delivered, was intended to compensate Barclays for the diminution in value over time of those securities, such

that what Barclays was receiving was the same seven billion dollars in value that it would have received if the transaction had been consummated as contemplated in September? Is that a fair way of thinking about it?

MR. HUME: Objection, Your Honor, just for the record. I think it misstates the amount of cash in the settlement, the 1.25.

MR. TAMBE: 1.25 billion.

THE COURT: Let's get the question right.

MR. TAMBE: It is 1.25 billion.

MR. HUME: I think you said -- well, the transcript says 1.5.

THE COURT: It says 1.5. Go ahead.

MR. TAMBE: Read the question back with that correction, please?

(Reporter reads back question)

THE WITNESS: I would say it's not a fair way of thinking about it, because the settlement, as I understand it, involves some cash and some securities. So the position that you would have to take is two positions.

One is that on the 22nd of September, Barclays would have known with great certainty what it was going to get in the settlement, the cash and the securities, and would've had an opportunity to hedge all those securities that it wasn't going to take possession of until a few months later.

Both of those were not true on December -- excuse me, on September the 22nd. So I would say no, it absolutely does not make sense to think of it in that way. The premise of your question is asking us to hypothetically think of a situation in September that wasn't at all true, at least, as I understand it. Barclays had no way of knowing exactly what that settlement was going to be.

What you might try to do, but I don't think this would get very far, is to think about, and I did mention this in my report, think about Barclays as having a claim, in some sense, an indeterminate claim against JPMorgan, and trying to sell that claim to some buyer on Monday, the 22nd of September. And I don't think there's any way that one could establish what a price for that claim would've been, but my knowledge as a financial economist would say that that claim would sell for a substantial discount from whatever you might have expected to get, if you could get determine what that is, because of a substantial amount of risk.

BY MR. TAMBE:

Q So -- but the way I described, the way of thinking about the claim as if basically giving them the value they would've received, had they consummated back in September, you're saying that's not a fair way to think about it, correct?

A Well, as I understood the question, and maybe I misunderstood it, but I understood the question to be asking

what would Barclays' value the claim that it got in actuality, the settlement, I should say, I shouldn't say claim, the settlement that it got in December, what it would have valued that in September, presuming that it knew that it was going to get 1.25 million (sic) in cash -- excuse me, I misspoke, 1.5 million (sic) in cash, and a certain set of securities.

And everything that I've read indicates to me that that was unknowable at the time.

Q My question is actually a very precise one and I want you to keep it in mind. In thinking about the December settlement, and how to value what Barclays received, would it be fair to think about the 1.25 billion dollars in cash consideration along with the securities that were identified, that that was intended to compensate Barclays for the diminution in value over time of those securities, such that Barclays is receiving the same seven billion dollars in value, assuming it's approved, and that the settlement is approved, that it would have received if the transaction had been consummated as contemplated in September.

Is that a fair way of thinking about it?

A With all due respect, I'm afraid I can't parse the question you're asking. I don't really understand. If what you're asking is, had it received seven billion dollars in September, which it had a claim for seven billion dollars, what would that have been worth in December. That would've been

worth seven billion dollars of cash put into the treasury market. It would've been worth a little bit more than seven billion.

Barclays didn't get, as I understand it, seven billion plus interest in December. So if that's the premise, and I may be misinterpreting your question, then I don't quite understand how that fits into the fact that they didn't get seven billion plus interest, but rather, and I think I misspoke when I said it last, now it is 1.25 billion in cash, and a certain set of securities.

Q Well, what Barclays was settling in December was the fact that they had a claim against JP Morgan and LBI for not receiving seven billion dollars in cash or securities, as of the closing date in September, correct, that's what they're settling?

A That's what I believe the settlement was for, yes.

Q But -- and they're also settling some of the stuff on the side, correct?

A I'm not sure what you're referring to.

Q Well, there was a pending litigation between Barclays and JP Morgan that was also resolved as part of the settlement?

A I believe that's the case.

MR. HUME: Objection. I have an objection, I think it assumes -- well, it's a question. I'll let the question stand, but I think it assumes facts not in evidence.

THE COURT: Are you referring to the separate litigation as part of the question?

MR. HUME: Yes.

THE COURT: I don't know about the separate litigation.

BY MR. TAMBE:

Q Do you know about the separate litigation, Mr. -- Professor Pfleiderer?

A Yeah, I'm afraid I don't -- I'm not sure I understand what's being referred to, so I probably should retract what I said and just say that I don't understand exactly what's being referred to. My understanding was simply that there was seven billion dollars in cash that was supposed to be delivered that wasn't delivered, and later it was settled in December, December 22nd for 1.25 billion in cash, plus a certain set of securities. That's my understanding.

Q Right. And then when that settlement was arrived at and presented to the Court, do you know what representations were made to the Court about how the Court should be construing that settlement?

A That I don't believe I know in full, no.

Q Okay.

MR. TAMBE: So can we go to the 12/22 hearing transcript, 12/22/08 hearing transcript on the settlement. And it's page 41. M-262, and it's page 41, line 21. And you can

start on line -- actually, start on line 15, please. This is the Court asking a question and making a statement.

(Pause)

Q Sit down. You may not be the right person to answer this question and Mr. Laraca (ph) might be. And I just want to know that before we close the record as to this aspect of the morning agenda, I would like greater clarity than I currently have on a valuation question. And this is not just addressed to you, it is addressed to anybody who can answer it.

I believe if I'm understanding the transaction correctly, that the working premise of it is that the 1.25 billion dollars in cash consideration, which is going to Barclays, upon approval, along with the securities that have been identified, is intended to compensate Barclays for the diminution in value over time of those securities, such that Barclays is receiving the same seven billion dollars in value, assuming it's approved today and consummated tomorrow, that it would have received if the transaction had been consummated as contemplated in September. Am I right in understanding that? That's a premise that I have, I just want to confirm it, and assuming -- and then assuming that's correct, I want to know what the current value of the transaction is.

Do you see that?

A Yes, I do.

Q What is your answer to that question as a financial

economist? Was the Court correct in its premise of understanding the structure of the settlement?

A Well, again, I wasn't there at the time, and I don't know how this settlement was determined, and I don't know what the intention of it was. What I do know, as an economist, is something of the following, which I can say to put some color on it.

If I had, say, borrowed a hundred dollars from you in January, and had failed to pay it in, say, July, and then I come to you in December and say, here let me give you some securities that are today worth twenty dollars, but in July were worth 500 dollars, you should be happier to get that than what you should to get a hundred dollars, because you'd be valuing it at the time that it was owed in July.

And from an economic point of view, that doesn't make any sense. Now, it may be that the characterization of the settlement in terms of how the actual value of it was determined, was determined with some notion of what that was, but as I would understand it at that time, JPMorgan could've simply written a check to Barclays for the total value of those securities, plus the 1.25, and Barclays would've been as happy or probably happier with that, because cash is better than the securities, because it doesn't have a liquidated risk and things of that sort of associated with it --

Q It takes two to settle, right? I mean, JPMorgan could've

written the cash, Barclays would've been happy to get the cash, but the reality was they were involved in a dispute, and this is how Barclays resolved the dispute. It elected to resolve this dispute by getting this cash and getting those securities, correct?

A But what I'm saying is that the value of what they got in the settlement is the value of what they got in December. And so if you look at what the claim actually paid off, as in terms of value, it was the value that was received in December, which could've been delivered in various ways. That's the point I'm making.

The value that was delivered could've been delivered as securities, it could've been delivered as cash. It could've been delivered in a number of different forms. And so the value that Barclays actually got, as a consequence of that claim, was what it got.

Now, the interpretation of how much they get could be along the lines that the Court was asked to understand here. So the Court's interpretation of how the settlement process worked is quite likely to be the correct one. But if you, as a financial economist, asks what was it that they got on December the 22nd, they got a certain value. And what that was worth in September is immaterial to what it was worth in December.

Q Okay. A couple of other follow-up questions. If they had, in fact, gotten all of these same securities in September,

you do agree with me that these securities declined substantially in value between September and December, did they not, sir?

A But here you have a very important distinction. Had they gotten those in December -- excuse me, I misspoke, September, they would've been able to trade those, they would've been able to hedge those. It's the uncertainty about what this claim was going to be in September that makes it, in my mind, inappropriate, among some other reasons, to value it as of September 22nd or September 19th.

Q Just focusing on my question and the securities. If they had gotten the securities in September, and held onto those securities, those securities would've declined substantially in value by December, correct?

A I think many of them would.

Q And well, it's not just many of them would, those were representations that were made to the Court in December, that the value of this collateral has declined substantially between September and December, correct?

A In the aggregate, I believe that that's true. And that's why I qualified and said, many of them would, some of them may have gone up, I don't know.

Q And those are not the only representations that were made to the Court to get approval of the December settlement. There were also representations made about how the Fed had valued

LEHMAN BROTHERS HOLDINGS, INC., et al.

those securities as of September, correct?
A I believe so. Again, I don't recall the actual testimony, but I think I may have seen it at some point, but I, sitting here now, don't recall the details.
Q And before we leave the issue of the JPM securities, you do understand that there are contractual and regulatory provisions that govern how someone like JPM values securities when it's dealing with the Fed, correct?
A I believe that's true, but I don't know all the details, no.
Q Right. And there's specific definitions of what is market value for purposes of their transaction, correct?
A Again, I believe that's the case, but I don't know all the details.
Q Okay.
MR. TAMBE: If we could pull up M-705, please.
THE COURT: While we're waiting for that to come up, since we started early today, I'm going to suggest that we consider a break sometime in the next ten to fifteen questions.
MR. TAMBE: Right after this set of questions would be perfect.
Chris, just enlarge the top of the page and it'll give us some context of what this document is.
(Pause)
BY MR. TAMBE:

Q You'll see there's an e-mail exchange between Shari Leventhal and Jonathan Hughes and you can scroll down, and I believe it may be on the second page. Turn to the second page, right. This is an e-mail from Shari Leventhal to Jonathan Hughes, the subject line is Barclays Chase, and what she's advising Mr. Hughes of is, this is the definition of market value used in the PDCF program. Do you see that?
A Yes, I do.
Q All right. And that's the Fed program, right, the Prime --
A Primary Dealer's Credit Facility, yes.
Q And that's the definition. Market value, the most recently available closing bid price for the particular security, as made available to the bank by a recognized pricing service which bank uses for pricing such security in the ordinary course of business, plus with respect to debt securities, any accrued interest on such securities, to the extent not reflected in such pricing, notwithstanding the foregoing cash shall be valued at face value.
Do you see that?
A Yes, I do.
Q And you have no reason to believe that that's not the operative definition of market value that related to the transaction that JPM was valuing assets for the Fed, correct?
A I have no reason to believe that that's not true, no.

MR. TAMBE: Your Honor, now's a good time for a break.

THE COURT: Let's break for 15 minutes.

(Recessed at 10:25 a.m.; reconvened at 10:53 a.m.)

THE COURT: Be seated, please.

BY MR. TAMBE:

Q Professor Pfleiderer, if you could turn back in the Barclays' demonstrative binder to slide 11, that's the GFS analysis. I just want to go back for a moment there.

MR. TAMBE: It's BCI 1103, page 11. And if you could just enlarge the numbers.

Q And just so -- so if I'm reading this right, what you're showing is the long positions in GFS are declining steadily from the 12th through the 19th, correct?

A In total, although I should note that, for instance, governments and agencies go up from, for instance, the 17th to the 18th, 36.44 to 38.19. But in the aggregate, if you look at the bottom line, they're generally declining, although even there, if you look at the 17th versus the 18th, you see it goes from 61.07, I'm looking at the bottom line now, to 61.44.

So it's not as we would say, monotonically declining, but it's generally declining.

Q And as a financial economist might say, the trend line is downward sloping?

A If you were to draw a trend line, it would be downward sloping here, yes.

Q All right. And again, I guess you'd agree with me that there are a couple of reasons for that. One is values may be falling, and assets may no longer be shown on the GFS inventory, correct?
A That would be the two major reasons that this would be occurring.
Q And by your calculations, according to GFS, as of 9/17 and 9/18, the total long position is about 61 billion dollars, correct?
A That is correct.
Q Now, one of the documents I'd ask you to look at was M-190. Remember that spreadsheet with the GFS data, that one?
A I believe so, yes.
Q We can enlarge it. We looked at that this morning, and this is Bill Parrinello sending back the GFS data, column K. Do you remember that?
A Yes.
Q All right. But this is being sent around on the 19th, the morning of the 19th, correct? So -- do you see that?
A Yes, that is the -- at the top, it says the 19th at 10:40.
Q Right. And so you have no reason to believe that on the morning of the 19th, the data that's being pulled from GFS is data as of the 12th, you'd expect the data to be pulled from GFS to be data as of the 17th, maybe the 18th, correct?
A I don't know precisely what was pulled, but I assume that

there was an attempt to pull whatever was latest.
Q Right, correct. And the table that we were just looking at, whatever was latest, if you were pulling on the morning of Friday the 19th, would be what, based on your understanding of GFS?
A Well, this would be -- the latest that was complete, as I understand it, would've been the 17th.
Q Right. And the reason you say that is, close of business 17th, open for adjustments through the day on the 18th, T plus 1, 6:00 p.m. on the 18th, you close down the numbers for the 17th, correct?
A That is my understanding, yes.
Q And therefore, if you're pulling the numbers on the 19th, that's what you're pulling?
A That would be my presumption, yes.
Q And so going back to your slide 11, as of the 17th, that number is 61 billion according to your calculations, correct?
A We do need to be very careful, we've taken out mortgages here, and added in the collateralized struction (ph) agreements, but that is what you get when you go to GFS on that date, taking basically the T plus 1 adjustments, subtract mortgages, and add in or keep in the collateralized mortgage or the collateralized search agreements.
Q And so just looking at the math then, if M-190 is adding up to about seventy-three billion and it's pulling data that is

as of the 17th or later, that's almost a twelve billion dollar delta from what you're calculating in GFS. You could add in the mortgages, you could subtract the mortgages, you're still going to have a pretty big difference there, aren't you, sir?

A I'd have to go back and look at what M-190 is precisely given -- gives, I should say, to put it in the context of what we're looking at here.

Q Now, going back to your comment about T plus 1, if I understand that correctly then, would it be correct, sir, that the prices that were as of the close of business on the 12th would not get locked down in GFS at the end of this process you described until Monday, 6:00 p.m.; is that right?

A That's my understanding, yes, correct.

Q Did you look to see and compare September 12th to September 11th, sir?

A I personally did not. I'm not sure that was done, no. It may have been done, but I did not look at that, no.

Q Okay. As you sit here today, you have no knowledge of that ever having been done by you or your staff, correct?

A I have no knowledge one way or another.

Q Okay. Let's move to a different topic. There was some discussion about equities yesterday. Do you remember that?

A Yes, I do.

Q All right. And in terms of the valuation difference, you'd agree with me that there are two drivers of the valuation

difference on the equities portfolio, correct?
A Two major drivers, yes, correct.
Q Two major drivers are date selection, 19th versus 22nd, correct?
A That's correct.
Q And the other is, what's the right liquidity adjustment.
A That is also correct.
Q Okay. And let's start first with the date issue, and you had a view on that, you expressed that yesterday in the transcript, you can go to the rough transcript 8585, I want to show you what you said, and then ask you some questions about that.
MR. TAMBE: And we may want to go up a page, please.
Q Starting with this question, line 8 down. You were asked a question, do you have an opinion as a financial economist of whether the September 22 closing prices was a reasonable way to measure the value of what Barclays actually received in the transaction. And you say it struck you as reasonable. And you're talking about the economics, and you said you were not commenting on the accounting, and what the appropriate accounting measure would be, correct?
A That's correct.
Q You go on to say Barclays did not have the ability to trade these until after, certainly after the open of the markets, and so the 19th was quite some time away from that,

and the ability to go back and trade something in past history when you didn't have possession of it, is something I don't quite understand, in particular, and I may just not understand the legal niceties of this, but as I would understand it, the possession would actually occur at the close of the transaction and --

MR. TAMBE: Scroll down.

Q -- not before, and I don't recall particularly exactly the time, but I think that was more like -- more 8:00 o'clock in the morning or so.

So from an economic point of view, I would think that you couldn't start trading these securities until then.

And you go on to say, now I may have the legal niceties there wrong, given how things are stated in the contract, and if I understand that better, I might change my economic opinion. But my understanding would be that they couldn't actually start trading things until the transaction had closed.

When did, in your view, Barclays get possession of the equities that are at issue in this case?

A Well, my understanding is, and again, I'm qualifying this and I actually having this read back, regret using the term legal niceties, because I don't mean that in any pejorative sense, but my understanding of the transaction is that until it closed, you wouldn't have operative possession of the securities and be able to trade them. That is my

understanding.
Q And maybe you're signaling something to me here by talking about operative possession. You know physical transfer of the equities took place Thursday night, the 18th, correct?
A That is correct.
Q Okay. So that's when the DTC transfers took place, that's when Barclays, as we've used the phrase, stepped into the shoes of the Fed, correct?
A That is my understanding, yes.
Q And, in fact, you have a slide that tries to identify the quantum of what moved over on the 18th, correct? And that's your slide 89. That's BCI Exhibit 1103, slide 89. And one of the things you break out there is the September 18th and 19th transfers, and you've got the Thursday transfers separated from the Friday transfers. The Thursday transfers, and again, I take your point, you were using nominal values, notionals, not market values here. Some ninety billion dollars of market value gets transferred Thursday night, correct?
A Again, not market value but notional value.
MR. HUME: Objection to --
THE WITNESS: I'm sorry.
THE COURT: There's an objection. What was the objection?
MR. HUME: I think Mr. Tambe just misstated market value, when he meant to say notional value.

BY MR. TAMBE:
Q It's only meant to show notional value.
A Yeah. That was --
Q 90 billion in notional value --
A What I was trying to say as well, it's ninety billion dollars or 90.6 billion dollars in notional value.
Q Okay. And you have tracked the transfer of the equities, haven't you, sir? You know the equities, eight billion or so of them came over Thursday night.
A That's my recollection, yes.
Q Okay. Now, your concern, and I guess this may be the question about legal niceties, is your concern is, well, they may have physical possession of it, but until the transaction closes, they don't have legal possession of it. Is that a question in your mind, sir?
A No. That's not what I'm actually --
Q What do you mean by operative possession then?
A No, that was not actually what I had in mind. My understanding of the repo contract is that you have possession of the securities, but it's a repurchase agreement, and so the borrower can repurchase those securities at the end of the loan period, be it overnight, or repo or whatever it is, the term repo.
So you have custody of those securities as collateral, but that doesn't mean from an economic point of view, you could go

out and sell those, and, say, convert it into cash without taking some risk, because you have to return those securities when the loan is paid off by the borrower.

So your economic position is quite different from actually having full possession of those securities and being able to do what with them what you want, without incurring any risk or liabilities.

Q Except if you've terminated the repo transaction, then you don't have any obligation to return those securities, do you, sir?

A My understanding would be that if the repo transaction was no longer in effect, then it depends upon how that comes about. I know that there would be legal considerations there, so I don't want to say anything about what the termination of the repo would -- the consequences of that, because that would involve some legal considerations as to exactly what happens in a termination of a repo.

Q Do you know one way or the other, sir, whether Barclays terminated the repo on Friday before this Court heard arguments on the sale order motion?

A My understanding was that due to a technical process, the repo was declared in default, but then the clarification letter basically made that null and void ab initio, so I think from the standpoint of thinking about the transaction, the repo was not terminated.

LEHMAN BROTHERS HOLDINGS, INC., et al.

Q Okay. Well, it was terminated and then unterminated, correct, mechanically speaking?

A That's right, but when you get to the 22nd, my understanding, and again, I'm put in a position where I'm asked to do something that I think is drawing a legal conclusion. But my understanding as a layperson would be at the transaction, given that the repo had been put back into effect, by declaring that the termination was null and void, that at the time of the transaction, it was still in effect. But that's just my understanding as a layperson.

Q And your understanding is, in fact, that with respect to securities that came over Thursday night, on Friday Barclays was already establishing hedges for many of those securities, correct?

A I believe there was an effort to do that, yes.

Q By the way, having terminated the repo on Friday, if the Court had not approved the transaction Friday night into Saturday morning, I guess a clarification could not have -- a clarification letter then could not have unterminated the termination, and Barclays would just be left with the securities and no LBI business, correct?

MR. HUME: Objection, Your Honor. I think, if I understand the question Mr. Tambe's, I think not for the first time, asking the witness to give a legal opinion.

THE COURT: Well, the witness is very clear in

answering all questions that he has answered as a lay witness, in respect to at least legal questions. And I think he's demonstrated his capacity to respond to questions such as this. But it is, however, a wildly convoluted hypothetical, and my suggestion is that it be restated.

BY MR. TAMBE:

Q Professor Pfleiderer --

THE COURT: Especially the use of the term unterminated.

Q Professor Pfleiderer, the state of play on Friday afternoon was, a termination letter had been delivered from Barclays, terminating the repo, correct?

A Again, that's just my understanding. I am basically using my memory here to remember some documents or discussion that I have seen somewhere, and I know that in the clarification letter, there was, I believe, an entry in that, that declared that that was null and void ab initio, I believe was the language. I may not be remembering it correctly.

Q But you would agree with me that the clarification only has life, if in fact, the Court had approved the larger sale transaction as a whole on Friday night?

A I don't -- that -- here we're on ground where you're asking for, I think, me to speculate on what would've happened in a circumstance, and how the legal environment would have changed, and I don't know. I really can't comment on that.

Q And we discussed incentives and motivations yesterday, but having taken possession of securities, having delivered a termination notice, do you have any views as to the incentives or motivations that Barclays may have had as it stood here on Friday evening, the 19th of September, 2008, seeking approval of the sale transaction?

A I'm not sure I'm understanding. You're conditioning it on the termination notice and asking how the incentives changed because the notice had been sent out. I'm not sure I understand the question you're asking me.

Q Well, as a financial economist, do you believe it would have had any effect on the motivation or incentives of Barclays, the fact that they had taken possession of, by whatever measure, fifty billion dollars' odd worth of collateral, and were hoping to get a sale transaction approved?

A Well, since you're asking about the specifics here, this actual occurrence, my understanding, which may be incorrect, is that the termination notice was in some sense almost automatically generated, so I don't think there was a conscious decision, I may be wrong, on the part of those that were making decisions at the top levels to terminate the repo.

And so since the incentives that you're asking about concerns those people that are making decisions about how to handle the repo and various other things, I'm not sure that, and I'm just to some extent speculating here, I'm not even sure

that they were aware of this termination notice, given that my understanding is that it was automatically generated.

So I am interpreting it -- your question is a hypothetical, if they'd understood and had the intent to terminate the repo, what would their incentives have been, and I'd have to really think that through before giving you a considered answer.

Q Well, with all other things being equal, they'd really want the transaction to be approved, wouldn't they?

A I'd want to think it through carefully.

Q Okay. In your report, in your original report, you had some discussion about how it is that Barclays and the Fed agreed to this take-out of the Fed. Do you recall that, and we can turn to that.

There's some specific phrasing you used that I want to ask you about. This is your expert report. I believe it's been marked as BCI Exhibit 341. It should be the first item in your binder. We'll pull it up on the screen, it's paragraph 13 of that report.

MR. TAMBE: It's page eight. The bottom of page eight, it's going to page -- numbered page nine.

Starting with, on the paragraph 13, the last line, so far as I am aware. Can you just highlight that, please? And then toward the end of that sentence.

Q You state, so far as I am aware, there is no dispute that

Barclays entered into the Fed replacement repo only because the Federal Reserve insisted that it do so as a condition of supporting the transaction. Do you see that?

A Yes, I do.

Q From whom did you get that understanding, sir?

A That was -- I'm not sure how I got that understanding. It was based upon various testimony that I had read, and basically it's a factual statement at the time that I made it. I said, so far as I'm aware, that was my understanding based upon depositions I'd read, and my understanding of the record.

It may have been a mistaken belief at the time, but that certainly was my belief.

Q And certainly while the views expressed in your report and your declaration is that Barclays was somehow an unwilling participant in this repo, it would not have willingly taken on this obligation, it wasn't, in effect, requested or required to by the Fed; isn't that right?

A My understanding is that the Federal Reserve did not want to basically stay in this position, having that risk, and had -- perhaps the word required is too strong a word, I'm not really sure, but, or insisted.

Q How about the word insisted?

A Insisted, yeah, I meant insisted was too strong a word, although that was my understanding, since it is a little bit different than required. But that there was pressure on

Barclays to take this position, to my understanding.

Q How about the timing? Do you have any sense, do you have any knowledge, does it enter into your opinion, whether Barclays was required to go through with the transaction on Thursday night, before the sale hearing, as opposed to after the sale hearing?

A I don't know how to answer that question without you telling me which opinion. I have several opinions.

Q Let's just say, do you have an -- do you have a view? Before we get to your opinions, do you have a view as to whether Barclays was required by the Fed, or that the Fed insisted that Barclays take out the Fed on Thursday night, prior to the sale hearing on Friday?

A Well, what I wrote here was that as far as I was aware, there was no dispute that Barclays entered, because the Federal Reserve insisted. I haven't read anything subsequent to writing that, to have changed that view, but I'm not absolutely sure sitting here today, that that's the correct view. But I can still say the statement that I made there, so far as I am aware, sitting here today, there's no dispute that that's the case, but I just may not be aware of something.

Q Have you read Ms. Leventhal's testimony from trial?

A I read her declaration, I believe I read some of her testimony, I'm not sure. I remember certainly reading a declaration that she filed with the Court, I believe.

Q Okay. And you'd certainly defer to Ms. Leventhal from the Fed as to what the Fed may or may not have insisted that Barclays do, correct?

A Oh, indeed I will, yes.

Q Okay. If you could turn to slide 58 in the demonstratives that Mr. Hume handed you. It's Exhibit BCI 1103.

On slides 58 and 59, you tackle this issue of the bid-ask spreads and the fact that data from December was used by Barclays to derive an appropriate bid-ask spread for the equities on September 22nd, right?

A I discussed the method that they used, yes.

Q Right. And that's not a methodology that you found in any written procedures and processes manual at Barclays, correct?

A I don't believe and I would be surprised if there was a written procedure that is addressing this particular issue, because it wouldn't have come up in the normal course of business.

Q And so this was devised as a one-off to deal with this situation, correct?

A I believe that in this circumstance, given the special nature of this transaction, they had to address a problem of how to determine how to adjust the equity prices to exit prices, and they had to use the information that they had at the time --

Q Right. That would be that process that you have devised

or used in the course of your work, have you, sir?

A I never had to do this type of calculation, no.

Q And what you did is you studied what Barclays had done, and you studied PWC's review of what Barclays had done, correct?

A I looked at what Barclays had done, and I --

Q Can you answer my question yes or no, you looked --

A I'm sorry?

Q -- at this and you looked at what PWC had done to review Barclays' work, correct?

A That is correct.

Q Okay. You did not try to replicate, go into the market and replicate this process to see if it produced skewed results, did you, sir?

A Well, I can't do that because again, the problem here is the question marks. So the question that you'd like to ask is, was this accurate. And to answer that question, you need to be able to fill in those question marks, and there's no way to fill in those question marks. We're trying to come up with a reasonable approach to make an estimate when we can't see, as I explained yesterday --

Q But my question, though, did you try to replicate what Barclays did? They did a look back process, did you try and replicate a look back process to try and validate their methodology?

A Make sure that the calculations that they made were correct?

Q Did you take this approach and run it with your own data set, where you went and collected data, in a live environment, and then tried to extrapolate it back to three months prior to see how it stood up to real observed observations from three months prior?

A So you're asking me did I do it with a live environment --

Q Yeah.

A -- from some time later?

Q Yeah.

A So, in other words, a live environment from today, for example, not today, but let's say in June of this year?

Q Well, there's one way you can do this, can't you, sir? You could go in the live environment today and collect a set of bid-ask spreads in the live environment. You can do that, correct?

A My understanding is you could do that, yes.

Q And you could wait for a month and go collect some quotes in a live environment a month from now for those same securities, correct?

A That is correct.

Q And then you could run this exercise that you have, you'd have the benefit of having live data both from the future point in time and the past point in time because you're doing a test,

you're doing a validation, correct? You could do that?

A Well, you could only partially do that. That's the problem, because there are question marks that come up here, and you're only getting part of the data. See, what is the problem here, is that you're trying to estimate adjustment for the entire portfolio of equities, which includes --

Q Let me stop you because you may have misunderstood my question. I'm asking you whether you tested the methodology, whether this was a robust methodology. You could, for example, go into the market today, not with these securities, find a hundred securities for which there's live data available, collect that data, store it, so you have real live data from the day. Wait a month. You've had several months in this litigation, wait a month, collect live data a month from now for those same hundred securities, no unknowns. Now apply the ratios and averages and see how well the ratios and averages work at predicting or providing a multiplier to look back one month. And now you have the benefit of having two full, complete sets of live data. Did you do that?

A No, because that wouldn't have been a test.

Q And did PWC do that?

A No, I don't believe that they did, and I'm afraid that you're failing to understand or failing to communicate is probably a better way to say it, what is the issue here.

That exercise that you talk about could indeed be done.

But it wouldn't be, in any way, indicative of the success of the approach that's taken to capture what you don't see, which is that the illiquid securities are not giving you the information, and those are going to have generally speaking, larger spreads, larger adjustments needed to mark down to an exit price.

And again, it's really the problem that when I was talking about yesterday, when I talked about Gallup poll not being able to contact people without telephones. But we're not going to be seeing the live quotes for securities, they're illiquid and not trading, or not trading frequently. So that's the problem.

So the exercise that you are proposing is one that could have been carried out, but it would not have answered the ultimate question, which is, is this a reasonable way to capture an estimate of live data, when you're not going to be able to see it even when you can access it, on all of the portfolio.

And that's why if you look at December 18th here, you'll notice that even in the accompanying live data, that the solid green is what we get, but the striped with the question mark is what we don't observe. And the problem is estimating what we need to do for what we don't observe.

Q But with respect to what's observed, two points, the 459 CUSIPs and the historical, you know that's what Barclays collected, but there was more historical data available from

Bloomberg and Reuters, correct? All you have to do is call them up and you'd get the data. You don't disagree with that, correct?

A I believe that Professor Zchemiasky was able to get more data than what Barclays was using, that's my understanding, yes.

Q If you ran the test, at least on the observed portions, you could test on the observed portions how good your model or methodology works with respect to the observed portions. You may still have the issues on the unobserved, but at least you can test the validity of this approach on the observed, and it doesn't work on the observed either, does it, sir?

A I'm sorry. I'd ask what you mean it doesn't work on the observed.

Q The fact of the matter, sir, is you're drawing a distinction between what's observed and what's not observed, and saying therefore, this is a pretty good methodology. The fact of the matter is, even on the observed data, this methodology doesn't work. It skews the results. You end up with wider bid-ask spreads than you have for the sample for which you actually have data. There's a mathematical problem with this approach, correct, sir?

A As I explained yesterday, and I had an example showing that Professor Zchemiasky's mathematical result is certainly correct and can happen, so I'm in no way saying that that can't

happen.

But what I'm saying and what I said yesterday, is that there are multiple issues here to address an appropriate adjustment to an exit price; and part of the problem is that you just can't observe data on those securities that are not liquid. And since those are part of the portfolio, you need to come up with a way to account for those.

Q So --

A So Barclays came up with a method, and my question, in my mind was whether that was reasonable to solve the overall problem, as opposed to just a part of the problem.

So if everything were observed, they wouldn't have had to do this, the problem was not everything was observed, and they approached this in a way that attempted to account for the various problems that you see here.

Q Other than the slide you produced yesterday, you've produced no calculations showing your testing of Barclays' methodology, to see if it made sense, whether it was a reasonable approach, whether it yielded reasonable results, correct, sir?

A Because I can't do that, and that's the point. Because you can't test something that you don't observe what you're trying to do here. You're just making an estimate based upon again, all this data here, which is striped with a question mark is something you can't observe.

Q Now, what you do offer in your slide yesterday was an example that if you put in the right numbers, gets you a result that validates Barclays' view, correct?
A That is correct. That is correct.
MR. TAMBE: Would you turn to slide 16, BCI 1103, please, and enlarge it. Please enlarge the numbers.
Q And what you did was, you put in what happens if we have an unobserved security C, correct?
A That's correct.
Q And then you inserted some hypothetical spreads for that security on each of the days, correct?
A That's correct.
Q And in each instance, you picked a number that was significantly higher than one as your hypothetical for unobserved security C, correct? Sixteen, fourteen and four are greater than one, correct?
A One percent?
Q Yes.
A That is correct, yes.
Q Okay. In picking that example, and showing this to the Court, did you try and fit your example to real-world examples of what distributions of spreads look like for large collections of securities, sir? Did you make any effort to do that?
A I'm not sure how I would've done that, because if we don't

observe the observe the spreads on the securities here, this is why it's unobserved.
Q You have seen Professor Zchemiasky's distribution for the 459 observed securities, correct?
A That's correct.
Q And that shows that the vast majority of the observations that you see are actually smaller than one, correct?
A And that again is because they are observed, and they, because they're observed, they're going to have lower spreads in all likelihood, because they're more liquid.
Q And you have very few outliers, correct, in that -- in the observed data?
A I'm not sure what you mean by outliers.
Q Well, numbers that are, you know, as high as four, five, multiples of that number.
A Again, that's to be expected, because this is a more liquid part of the spectrum.
Q And in any of your analysis, you didn't try to collect from market participants or from market studies, any kind of hard data that would give you an indication of what reasonable spreads ought to be for the unobserved positions, correct?
A I did not and --
Q Well, you did not, PWC did not, and as far as you know, no one at Barclays did either, correct?
A Not that I'm aware, no.

MR. TAMBE: Give us slide 61, please.
Q You do make some comments about what it is that PWC did. You don't have a similar slide that says what steps you and your staff took with respect to these equities, do you, sir? There's no similar bullet list of here's what we did?
A Did in what sense? I'm sorry.
Q Analytics.
A So analytics, in terms of --
Q Other than just reading the documents, did you test the methodologies, did you test the prices, did you do any of these things that Barclays did or PWC did or didn't do?
A I did not replicate what Barclays did, nor did I replicate what PWC did, no.
Q The third bullet point which talks about audit sampling, that's a reference not to spreads but to prices, correct?
A That's correct.
Q Okay. So they're going back to prices and you don't think there's any dispute in this case, putting aside the date issue which you're picking the 19th or the 22nd, there's no dispute about what the price data set looks like, correct?
A I don't believe there is, no.
Q All right. So let's put that away. The bottom bullet point, you suggest that what PWC did, was did additional audit procedures on the bid-offer adjustment, considered further scenarios to adjust for illiquid positions, and this produces a

range of 373 to 453.
Those additional audit procedures, no part of those procedures dealt with adjusting the 4.34 multiplier, correct? It all dealt with how you would further increase that multiplier for the illiquids.
A I'd have to go back and look at it. Sitting here today, I don't remember precisely what they did.
Q Now, go to the next page, 62. The first point there, you observe from the PWC papers is September spread should be wider, due to the prevalent extreme market conditions. Right. And that's a relative statement, should be wider than December, correct?
A I didn't interpret that as what they're saying, that's implied, but I'm not sure, maybe they're saying should be wider than normal, but I think it's referring to December.
Q And you know that not to be true, correct?
A I'm sorry?
Q You know that's not true.
A I know that for the samples that they observed, which was liquids, there was a difference, and it was in the direction of December, I believe. But I think here what they're doing, is they're referring to the entire equity portfolio and not to that sample.
Q And, in fact, not only did the data set that they used or selected show greater spreads in December than September, that

was the general sentiment of the market, as you went through the fourth quarter, right, volatility increased dramatically after the closing of this transaction.
A In fact, we looked at it yesterday, how it increased dramatically and then it came back down in December. Not to quite as low a level as I recall as what was in September. The highest volatility, as I recall, was in October and November.
Q Okay. So if we could look at that, 946, BCI 946.
MR. TAMBE: And if we could just increase the numbers.
Q And you agree with me, this is what you call the fear index, right, the VIX index?
A That’s what people call it, yes.
Q Well, you called it that, too.
A Yeah, I did say it is called the fear index.
Q Okay.
A I usually, if I’m teaching, though, I call it the VIX.
Q Okay. On -- September 22nd is shown there, and it’s somewhere below the thirty-five line. Do you see that?
A That’s correct.
Q And then when you get to December, you are talking about December 18th, somewhere in the middle of that last column, you’re talking about volatilities in the forty-five to fifty-five range. Do you see that?
A I’m not sure exactly where it would be, but it would be somewhere in there, yes.

Q This goes higher --
A It is higher, but --
Q -- than September.
A -- as I was saying, it is not as high as what it was in October and November.
Q So to the extent there's a statement being made by PriceWaterhouse that the September spread should be wider due to prevalent extreme market conditions, that data, at least, seems to undermine that conclusion in some way, correct?
A Well, the observation I would make is that, yes, indeed volatility had gone up, and as a financial economist, I would say that spreads would tend to go up with volatility, but there are other considerations as well, in terms of what determines spreads. So it is not a simple relationship between volatility and spreads, and here's where I think we get into the issue of does someone who's there trading in the markets, has a feel for the markets, and gets some information, basically Barclays and PWC were making judgments based upon their quote/unquote feel for the markets at various times.
Q Right. A feel for the market is an important issue for you, correct?
A It was an important issue in the sense that going back and making estimates of what liquidity adjustments would be or what pricing would be requires someone to have some understanding of what market conditions were there. What we're looking at here

does measure something about market conditions, but doesn't necessarily capture all of the important characteristics of the market in any particular point in time.

Q And you wouldn't describe yourself as someone who has market feel in all of the complex securities that are at issue in this case, correct?

A Indeed, I wouldn't, and that was one of the reasons that I didn't think it was useful to me. I think I explained this, to go back and do a valuation of my own, because I would not have today the feel for the markets, and my judgment today or back in December would not have been better than the judgment of the Barclays personnel who were doing this in the price testing, and being audited by PricewaterhouseCoopers.

Q Right. The Barclays' traders weren't the only traders in the market. There were all sorts of traders in the market, who had better market feel for what was going on then than you do, correct?

A Oh, indeed. I, being an academic I'm not trading in the market every day, so I don't have that knowledge that a trader would have.

Q So someone who has traded and valued and risk managed fixed income assets for three decades is likely to have a slightly better feel for the market and those securities than you do?

A That's possible, it would depend on the individual, but as

a general proposition, that could be true.
Q And that market feel would give them a position to make reasoned rational judgments about bid-ask spreads and volatility in prices, correct?
A Correct with the qualification that we could get five people in this room with market feel, experience, put them in five different rooms and they would come up with different judgment, and that's why I said that as we move across this spectrum, from the green to the red, some element of judgment comes into play. There is no absolute correct answer here. It involves some judgment.
Q But all the things being equal, someone who has trading experience, in your view as a financial economist, has a better sense of market feel than someone who doesn't?
A Yeah, given that you said all the things being equal, I'd have to agree with that, yes.
Q Right. In terms of the review and the work you did off the Barclays' materials -- I'm sorry, the PWC materials, at the time of your report, you hadn't spoken with anyone from PWC before rendering your opinion, correct?
A I believe that's correct. I'd only spoken with Barclays' personnel.
Q And as of your last declaration on September 1, you had spoken to Barclays' personnel who had been in touch with PWC, but you made no statement in that declaration that you had had

discussion with PWC, correct?
A I personally have had no discussions with an individual from the PWC.
Q Okay. So, Mr. Hume had laid out here, I think ten large banker boxes, you weren't here that day, but there were large banker boxes of documents from PWC. I take it in your review of those documents, you personally didn't feel the need to speak directly with someone at PWC to understand what was going on there, correct?
A I basically read the documents and took them for what they were and didn't speak to anyone, yes, that's correct.
Q And the people at Barclays --
A Can I qualify? I did not read all the documents. I want to emphasize that I read quite a substantial number of documents, but I think that the percentage, it probably wasn't as great as -- I certainly don't want to misrepresent that I read all ten boxes.
Q And in terms of what PWC did, they performed an audit, correct?
A That's my understanding, yes.
Q It's not your understanding that PWC here was asked to do an independent CUSIP-by-CUSIP valuation of the securities that had come over, correct?
A I don't believe that was what they were charged to be, no.
Q And, in fact, what they were doing in this matter, in

reviewing this transaction, was part of the audit of the financial statements of Barclays, correct?
A That is, I believe, yes.
Q And this wasn't a special assignment in any way, you got your audit responsibilities to come in here and help us do something special with these transactions, as part of the annual audit, correct?
A That is my understanding, yes.
Q Now, you know that the PWC papers are replete with statements by PWC that management said this, and specific people at management said that, et cetera, correct?
A That is correct, yes.
Q And that's consistent with your understanding again, not as an accountant, but as a financial economist, that financial statements are the responsibility of management, not the auditors. It's management who's providing that information, correct?
A I believe, and I may be characterizing this incorrectly, but I believe that management signs off on the accounting statements, and are basically, by signing off on it, asserting that they are true and correct, at least they've been prepared according to generally accepted accounting principles.
Q And there's a statement that PWC makes when it's concluded an audit about what its audit means, correct, as a little as almost boiler-plate type language that appears in financial

statements.
A I believe that's correct.
MR. TAMBE: If we turn to M-554, page 178, keeping rolling down, you're on page 159. There we go. And that will need to be enlarged, please.
Q And I've just pulled up on the screen the statement made by PWC in connection with the Barclays' 20-F. All right. This is a statement they made. And starting with the fourth line down, towards the right, these financial statements.
And it reads, these financial statements are the responsibility of the company's management, our responsibility is to express an opinion on these financial statements based on our audits conducted. Our audits of these financial statements, in accordance with the standards of the Public Company Accounting Oversight Board of the United States.
And you've seen that abbreviated as PCAOB, correct, from time to time?
A I believe so. I can't assert for sure that I've seen that abbreviation, but I believe so.
Q And then it goes on to describe what those standards are and what the audit really is. Do you see that?
A Yes, I do.
Q As part of those auditing standards, the PCAOB standards, does the information or a rationale that's offered by management have to be convincing for PWC to accept it, or can

PWC be satisfied with allure of standard of evidence or rationale offered by the client, do you know?
A I don't know the precise threshold and how it would be said, so I wouldn't want to say something that is not in accordance to what actually is said.
Q And you did see from time to time --
MR. TAMBE: You can take that down.
Q You did see from time to time in the various PWC papers, statements about PWC not taking exception with something that management has suggested or proposed?
A That's correct.
Q Okay. And Mr. Romain testified that accountants were masters of negative assurances. Do you remember reading that?
A I do remember reading that, and it's certainly in accordance with my reading referenced statements that PWC makes.
Q And you saw no statement in any of the PWC papers that you looked at, that says, we've reviewed all the valuations done by Barclays, and we agree with each of the values ascribed by Barclays to each of these assets?
A I believe that the term is used, and I can't say that it's used everywhere, but the term that's used often, is that we found this reasonable, or we do not find this not reasonable, I think is sometimes the double negative that they put it in, but basically they're looking for processes that have been

following, and asking the simple question, are these likely to produce reasonable results.

Again, we get back to this notion that there's a fair amount of judgment involved in assessing these values, and I think that PWC, as I understand it, is asking more reasonable procedures follow, especially in those situations where some judgment is involved, that are likely to produce reasonable results. Now that language may not be used in the precise way that I stated it, but that's my understanding of what they're doing.

Q Right. And for that process to be a meaningful process, that would be a process by PWC, you'd agree with me for the kinds of assets we're talking about here, PWC needs people who have the same or better market feel than the folks at Barclays for making those judgments, correct?

A I would state it a little bit differently. First of all, I know that they had people that -- I forget the name of the group, it was a special -- actually I can't remember now, it had an acronym, and I just can't remember sitting here right now -- a group of people that, for example, did the -- review the fixed income valuation that was done in various settings.

Q Well, what do you know about those group of people? Do you know anything about them?

A I don't know anything -- I don't know who they are by name or what their FON (ph) for days are, but what I do know, and to

respond to your question, it's not even necessary that PWC people are better than Barclays --

Q Or as good as.

A Or even as good as. What you're getting is an independent opinion which provides some additional information. So you've got a process where --

Q Can I just stop you there for a second.

THE COURT: I think you should let the witness finish.

THE WITNESS: You have a process where people in Barclays are basically doing their best to come up with values, and other people outside that have a great deal of expertise, they may have different knowledge than the people in Barclays who are reviewing it, and so you're bringing some more knowledge and expertise into the process. And the outcome of that generally is going to be more reliable numbers, not always, but that process is set up to be one that produces a more reliable outcome.

BY MR. TAMBE:

Q And just so I understand then the various steps in the process. It starts with, I guess at the very beginning, it starts with traders at Barclays taking these assets onto their books, and ascribing some values to them, correct?

A Well, I want to be a little bit careful in answering that. In the normal course of business, you would have traders who are in the markets, who are acquiring and selling assets. This

transaction turns out to be quite different. It wasn't that particular trader sitting at a particular desk said, I want to buy this particular security from Lehman. Instead, a bundle, a portfolio of securities came in. They were allocated to desks, there were some internal sales, but it was a slightly different process than in the normal course of business.

So with that caveat, I'm not sure whether what we were talking about was the normal course of business or this particular transaction, which was a little bit different just by its very nature than the normal course of business.

Q Well, let's talk about this transaction, though. So in this transaction, even though the way the assets are acquired is different, in the sense it's not individual desks doing trades, there's a lump of assets that comes over, there was some trader involvement at the outset, correct?

A The traders had input into the process, definitely.

Q And so they exercised, you would expect, some market feel and judgment in those initial assessments of value.

A That was my understanding, and again, that's why I didn't attempt to do it myself because I wasn't there in the markets at the time, and they had traders that were there that had knowledge that I certainly do not have.

Q And among the traders that you may have heard of or spoken to, Mr. King and Mr. Yang, correct?

A Those would be two in the PMTG Group, yes.

Q The PMTG Group that deals with the mortgage-backed assets, correct?

A Basically they deal with the more difficult to value assets. Many of them involved mortgages and real estate, but not all of them.

Q And so their market feel and judgment would be especially important in terms of assessing the values of those difficult to value assets, correct?

A They had knowledge that would be useful in adding to the mix of information that’s used in this process, yes.

Q That’s level one.

A However --

Q And this is called that level one. It’s the first exercise --

A Could we not call that level one.

Q You’re actually right, I shouldn’t use level one. That’s step one.

A Step one, yes, much better.

Q Good point by you.

Step one, you’ve got the traders; step two, PCG comes in behind the traders and does, what you call this independent price assessment, correct?

A The PCG Group within Barclays that's going to, again, in the normal course of business would be reviewing the trader’s marks.

Q And they're exercising judgment as part of doing that as well, correct?

A They're exercising some judgment and getting some additional information, that's correct.

Q Okay. And then when PW -- when PCG is done, the PWC comes in, and PWC exercises judgment in terms of how it reviews the judgment exercised by PCG, and in turn, the judgment exercised by the traders at Barclays; is that right?

A That's correct, but I would like to add one caveat here. The process that you described makes it sound like it's a sequential process. And my understanding is, at least in this particular case, that PWC was involved not as coming in at a final point, and looking back on what had been done, but rather was actively involved in a more dynamic process, so that when various procedures were proposed or were being used, PWC could push back or make suggestions and Barclays could then make changes.

So the only change that I would make to your description is simply to say that it's not necessarily a sequential process when step one is done, and then step two occurs, and then when step two occurs, then step three occurs.

Q Fair point, that it's given that the unique nature of this transaction, you have these various exercises of judgment, so almost happening one on top of the other, correct?

A That's more correct than saying it was sequentially, yes.

Q All right. And it's not just PWC that is involved at an early stage in this process, you also have a situation here where the traders remain involved and in contact with PCG and PWC at least through December, correct?
A I believe that's certainly true. I believe it certainly -- I believe Jasen Yang was in contact with PCG. There's an interplay there, definitely.
Q And on the things that there's interplay about is stress, liquidity discounts, prices; correct?
A Those would be some of the things that would be the technical information that one needs to establish reasonable marks for these assets, yes.
Q Okay. So we've got traders exercising judgment, you've got PCG exercising judgment, you've got PWC exercising judgment, and on top of all of that, we've got you, Professor Pfleiderer, exercising judgment over their exercise of judgment; is that right?
A I would characterize it differently. I wasn't certainly involved in the process that led to the acquisition balance sheet. What I did is look at what was done by Barclays, and looked certainly when I got them and all the PW -- well, no, scratch that, not all the PWC papers, but many of the PWC papers, and satisfied myself that this was a process that was going to produce a reasonable valuation that would be an upper bound on the economic value of these assets.

So that was the -- while I don't think that I was a sequential part of this process that led to the acquisition balance sheet, certainly I was not that.

Q The phrase you use that I want to come back to, you said an upper bound on the economic value of these assets. You're not expressing any opinion as to the upper bound of the fair market value as measured in accounting terms of these assets, are you, sir?

A Well, here we get into -- I certainly -- let me give a quick answer to that, no.

I'm not opining as an accountant. When we use the term fair market value or economic value, we again have to go back to my discussion yesterday of whether you're looking at individual CUSIPs, CUSIP-by-CUSIP or whether and for this transaction it's very important when you're considering the totality of the whole portfolio.

So I would be careful, or I wouldn't be careful when we use the term fair market value or economic value, we specified which of those we're talking about, but certainly I'm not, in any way, opining on the accounting that was done and whether it was done correct or done according to generally accepted accounting principles.

Q Thank you for answering my question, but the last part of the answer causes me to go back and make sure we're not talking past each other.

You're not expressing an opinion that the value that's been arrived at that's on the acquisition balance sheet, is an upper bound of the accounting fair market value for those assets, are you, sir?
A Again, if it's construed as my expressing an accounting opinion, no.
Q Thank you. Can we turn in your expert report, BCI Exhibit 341, to paragraph 51, please? Page 30 in the document.
MR. TAMBE: If you'd go back, if you would -- just highlight 51, please.
Q And in 51 you sort of lay out several parts of your analysis and what you looked at, correct?
A What I said is based on some investigative work, and my understanding of what was done, I believe the following are key aspects of the process by which Barclays developed exit price marks.
Q So this is the process that Barclays follows to get exit price marks?
A And this is my understanding at the time I wrote the report, yes.
Q Let's turn to subparagraph 11, please. And in subparagraph 11, you recognize that there is a connection between how you value these assets, the Lehman assets for acquisition balance sheet purposes versus a potential impact that the valuation could have on trading profits and losses in

subsequent periods, correct?

A That's correct.

Q And as a financial economist, to the extent you have traders involved in the valuation process, you would expect the financial incentives to be such that they'd want to minimize their trading losses, and maximize their trading profits, correct?

A Well, I would have to point out, ultimately I would think that their incentives are based upon how their compensation is determined. And so I would need to know, basically, how the trading profits relate to their compensation. Generally speaking, their bonuses they're given as I understand that have some relation to their trading profits, not necessarily completely defined by that, is my understanding, but I don't know in the case of Barclays exactly how their compensation works.

So I would -- to make a definitive statement, I would need to know a little bit more.

Q Now, you have no reason to believe that Barclays compensates its traders differently than most Wall Street firms, do you, sir?

A I have no knowledge one way or another, no.

Q And in terms of compensation, it's not just some of the trader's compensation that comes out of bonus, it's generally the case, is it not, that most of the compensation comes from

the bonus pool?
A My understanding is that is correct, yes, at least for most traders, yes.
Q As directly linked to profit and loss for that trading desk on which that trader works, correct?
A Well, no, that was what I was not willing to say with a definitive statement, because when I say directly it could be indirectly. So, in other words, I think I know what this relates to, the movant's, I believe, are going to assert that the traders had an incentive to mark things low to get high profit.
The question is, whether that would ultimately because of the direct relation with their compensation, result in higher compensation, and there's a certain linkage there, and I just don't know how that works within Barclays. So that's why I'm being careful.
If you tell me that or if Barclays were to tell me, or I would see evidence that there's a complete linear relationship, for example, between trading profits as measured by the accounting systems and their bonus, then that would be one situation. If there's some judgment that's being made, then that linkage is not as direct, and then we have to think more carefully about what the incentives are.
Q Okay. And in the course of all the work that you have done in this case, you didn't ask Barclays what its incentive

compensation plans are for traders, especially the traders who were involved in this valuation exercise, did you, sir?

A I personally did not, no.

Q Well, not only did you personally not, you're not aware of anyone on your staff having done so, are you, sir?

A I don't know. Someone may have had and I don't know about it.

Q Just one question on policies and procedures, or a couple of questions on policies and procedures.

You have commented from time to time in your expert report, probably yesterday in your direct as well, that there were policies and procedures that were followed by the PCG Group in Barclays in coming up with values, right?

A I believe that Barclays has not denoted, Barclays has various policies and procedures, and my understanding is that they made every effort to follow those in this particular transaction, but because this transaction was a unique transaction, having some characteristics that were not in the normal course of business, they had to, in some cases, have followed policies that may not have been contemplated, or may not have been in the books before, just because of the unique nature of that transaction.

Q And while the example of that was, what we talked about earlier, the adjustment that was made for liquidity in the equities, correct? That was --

A I believe that would be a good example where they had to do something just because of the nature of what they were having to do, that wasn't similar to what they did in the normal course of business.

Q And in that type of exercise for liquidity adjustments, was also used for agency RMBS and treasuries. And when I say that type of exercise, they had to devise a way of calculating spreads, correct?

A In the case of most of these assets, they had to determine how to basically make sure that they were marking down to an exit price, because my understanding, which I don't think it is at all contested in anything that we've been discussing, is that the accounting requires them to mark to an exit price.

Q Right. And as part of that process, they would start by calculating spreads, and in calculating those spreads, they're not reading something off of a policy manual or a procedure, they're devising a methodology to deal with this situation and these circumstances, correct?

A Well, certainly the case if there's no policy manual that says that you should use a spread of four percentage or three percent, because the spread in the adjustment is going to depend upon market conditions. So the policies don't give you actual numbers to use. They tell you how to basically follow policy to get reasonable valuations, given the right circumstances.

Q Well, the policies don't give you mathematical formulas, into which you can plug data in either, right? They don't tell you one approach, for example, for equities is, you take a date out of December and you roll something back three months. There's no level of detail like that in the policies and procedures manuals that you saw, is there, sir?

A Well, again, we weren't even contemplating seeing something like in the policy and procedure manual, because that was not something that was encountered in the normal course of business.

So I would've been very surprised if I picked up the policies and procedures manual, and said -- which was written, let's say, in January of 2008 and there was a section that said, if you acquire in a large transaction, the trading portfolio of Lehman Brothers, here's what you do. So it didn't surprise me at all that there were some idiosyncratic elements that had to be addressed here, for which there wasn't a simple policy that was written.

Q Another issue that comes up in the valuation, and especially the valuation of this Lehman collateral that's come over to Barclays is to compare and see how you're pricing this new collateral to existing collateral that's already in your books of a similar nature, right?

A I'm sorry, could you read the question back? I was just thinking of the last answer I gave, and wanted to make sure

that I'd said the right thing, which I'm now sure that I did, but I'm sorry, I missed your question.
Q Okay.
A I apologize.
Q I'll try. One of the issues you'll agree with me needs to be looked at when you're taking on board a large set of securities and pricing them, is to see if you're pricing them in a manner that's consistent with how you've priced other such securities already on your books, correct?
A That would generally be the case. And indeed I saw, in various parts of the PWC work papers, specific references to the fact that Barclays was using similar procedures to value the acquisition portfolio to what they call the legacy portfolio. So if you search the PWC work papers for the word legacy, you'll see that quite often or fairly often, they're comparing the procedures that are being used in this idiosyncratic transaction, huge idiosyncratic transaction, with what was done to value things in the legacy portfolio, which means the Barclays' assets that were already there. And noting that generally speaking, that similar procedures were being followed.
Q And so they were reviewing all procedures, not the outputs, not the prices of values actually assigned to those securities. You may have the same CUSIP on Barclays' book, one legacy, one new, valued at two different prices, correct?

A That's potentially possible, but I haven't seen specific evidence that that occurred, but it's potentially possible for a CUSIP to have two prices assigned to it.

Q Are you done? I'm sorry.

A Yes, I am. I'm sorry.

Q As part of your analysis, as a forensic economist into the reasonableness of the value, did you do any analysis to see how Barclays had valued these securities, the Lehman securities compared to how they had valued legacy securities?

A Let me -- to clear the record, I don't -- maybe I'm considered a forensic economist, but I just consider myself a financial economist that's been brought in to do this. I just don't call myself a forensic economist.

Q No, that's my mistake.

A No --

Q I misspoke, a financial economist.

A Anyhow, I just wanted to make sure that it was understood that this is not what I do for a living.

So the question is, did I do that exercise of looking at it, the answer is no.

Q And not only are you not a forensic economist, you're not a forensic accountant either?

A I am even less a forensic accountant than I am a forensic economist.

Q In the course of the work you were doing, and you've

described aspects of this work, the review of the PWC papers, conversations with Barclays, did you speak with any of the Lehman traders, who had placed some of these positions, and while presumably now employed at Barclays, to see how they would describe these transactions to get some market feel?

A No, I did not.

Q Did anyone on your staff do that?

A I would have to check. I know that my staff spoke with many people -- several people at Barclays, and I'm not sure whether they were Lehman, I forget if the term should be legacy Lehman or legacy Barclays, whether they came over with the transaction from Lehman, or whether they were legacy Barclays traders, so I don't quite know how to make that distinction.

Q You described, I think yesterday, that you spent time talking to people at Barclays, but that your staff had spent many, many more hours in those discussions. Is that fair?

A I think that's fair. I don't know the precise number of hours. I know what I spent, which was several hours in December talking to Gary Romain, Sean Teague, Rich Landerman (ph) -- Washdel, I forget his first name, I'm sorry, I apologize, I don't recollect his first name, but I talked to several people, yes -- and Jasen Yang, Stephen King.

Q Well Mr. Washdel may be one that you didn't actually speak to.

A I'm pretty sure I did, but I may not have. I'd have to go

back and review.

Q So you spoke to those individuals, and I assume that your staff spoke to many more individuals for much longer periods of time, correct?

A I know that they spoke with those people and perhaps some others, much more. I can't quantify what the ratio is, but I know it's a fairly large ratio of the time that they spent talking to the time I spent, yes.

Q And given your direct testimony yesterday, along with the work that you've done, these are not chats, these are really detailed conversations on the real nitty gritty about how bid-ask spreads come about, how prices come about, all this stuff, right?

A That is correct, yes.

Q How is it that your staff conveyed to you the results of their conversations?

A Mainly verbally. We would sit down and go through, go through -- we met in Palo Alto a number of times and talked over the phone.

Q But you understand there's no notes, no writings?

A There may have been some e-mails, but most of it was in meetings that we had in Palo Alto and in conversations with Romain and -- and work that we'd done in, when we were sitting in the same room.

Q I know from your deposition that you did not take any

notes of any of the conversations that you had with the people that you spoke with, right?

A That's right. When I was speaking to Gary Romain and others, I was not taking notes.

Q And I know no notes have been produced to us that were given by your staff to you describing their conversations with staff. How do you do this in a conversation, sir? How do you get through 12,000 CUSIPs, the most complicated securities, and it's all done orally, and that's how you come to your conclusions?

A Well, first of all, I didn't do CUSIP-by-CUSIP, so there wouldn't be 12,000 different conversations. There were questions that came up, where I had questions about various things, and I think they were probably at least maybe 30 or 40, I'm just guessing, but at least 25 or 30 questions that I can probably remember asking about various things.

And staff would contact oftentimes Sean Teague, or I think Gary Romain, but mainly Sean Teague I believe, and find out answers in terms of how things were done and then report back to me.

Q And again, all orally, not in writing.

A Well, usually it was -- at least some of those questions would relate to how to do the various analysis that was being done, and understanding just how to navigate through the spreadsheet, and basically where calculations were made and

things of that sort. So staff would find this out, and then we would sit down, and oftentimes again in Palo Alto we would go through the spreadsheet, and I'd have some more questions, and some more questions would be answered.

Q Okay. And just so I'm clear, you would not write down the answers, and your staff would not write down the answers?

A Staff may have written down the answers. Once I saw how it worked in the spreadsheet, then I had an understanding, and we could go forward.

Q And did you rely on any of those writings by staff to form your opinion, sir?

A No, I did not.

Q So whatever they wrote down, you didn't look at it?

A Certainly not when I wrote my report or declarations or any other things I've done.

Q Let's change topics. Let's talk about the Giant Stadium.

A Okay.

MR. TAMBE: May I just have one moment to grab my --

THE COURT: Sure.

(Pause)

BY MR. TAMBE:

Q And again, let's start with your testimony yesterday about the Giant Stadium marks. And, in particular, in the rough transcript, it's on page 8626 at the bottom over on to 8627, and while that's loading up, let me give you some context.

You were obviously -- you disagree that the valuation that movants had put on par on the Giant's Stadium bonds, correct?

A Yes, I do.

Q And one of the questions or statements you made yesterday about why you doubt the valuation of par, has to do with, well if they're valued at par, why didn't Lehman sell them before bankruptcy. Do you remember that?

A I think that's an interesting question to ask, certainly.

Q Yeah, that's a question you asked yesterday, so let's highlight that, and the answer starting on line 17 down over on to page 8627.

MR. TAMBE: And if you could pull up the rest of the answer, please.

Q You say, did I say September, I meant to September, 10th of September. So before the bankruptcy, some time before the bankruptcy, Lehman Brothers is in fairly desperate need of cash, it's got a liquidity crisis, among other things, so if it could have sold the Giants' bonds at par, and this of course, was before the market turmoil, you would think that it would have even a better prospect of selling them before than as things developed.

Then there's an interesting question why didn't, because this would've solved, at least to some extent, its liquidity problems by being able to sell these for their full value. And the fact that they didn't, I think additionally calls into

question this proposition that they could be sold at par.
That was your testimony yesterday, correct?
A That is correct.
Q Okay. Pre-bankruptcy of Lehman Brothers, sir, who bore the risk of the floating interest rate on the Giants' Stadium bonds?
A So my understanding of the transaction was that the bond, as it was actually held by the Giants was basically a fixed rate bond, because the Giants were paying floating to Lehman Brothers, but then there was a fixed or floating spot in effect.
Q You may have that backwards. They were paying fixed to Lehman Brothers, receiving floating from Lehman Brothers.
A Well, no. I believe that they were paying floating, and then Lehman Brothers would pay the floating to the Giants, and then the Giants would then pay fixed. There were two parts of it.
The bond required the Giants to pay floating. They basically -- when I say floating, what I mean is the auction rate that's been determined, which is intended to be a floating rate. So the Giants had to pay floating to Lehman Brothers. If that was all the transaction, then they would be paying floating. But Lehman Brothers entered into a slot in which Lehman would pay floating to Giants, and then Giants would pay fixed.

So when you add that all up, it looks a little bit strange. It turns out that the Giants are paying fixed rate, of I think it was 6.55 percent, I may have that wrong, to Lehman Brothers.

Q And Lehman Brothers will in turn, is paying the floating rate?

A That's correct.

Q Okay. And if Lehman had sold the bonds to a third party, that third party would have the right to receive the floating rate, correct?

A The third party would have the right to receive the floating rate, and Lehman Brothers could potentially have sold or traded position in the fixed for floating spot, to get rid of that liability as well.

Q Right. So given all the turmoil in the auction rate market, in 2008 -- well do you think Lehman would've had an easy time selling that bond?

A Well, that's exactly the point. That's exactly the point I made.

Q That's your point. The point is it's difficult to sell the bond.

A Exactly. That is precisely the point I made. In other words, with the marking it to the par, assumes that the bond is easy to sell. And the point that you just raised is exactly the point I'm trying to make.

Presumably, Lehman couldn't sell that bond or didn't sell that bond, because it was difficult to sell, and that's why you wouldn't mark it to par. So that was the point --

Q So that was the point.

A -- that I was trying to make.

Q Here's the point. If Lehman sells the bond, it also has to sell the slot, correct?

A So the slot is part of that bond, but the notion that the markets are liquid at this time would indicate that it shouldn't have any trouble selling that. In other words, the notion that there's liquidity here that allows these transactions to occur, and things can be marked at par, is called into question by the fact that Lehman Brothers isn't able to disentangle itself and get full value from this bond.

Q Yeah, but the disentanglement ends with the filing of bankruptcy, because the swap gets terminated or the swap no longer exists, correct, sir? That's a changed circumstance, post bankruptcy, but pre-Lehman/Barclays' transaction, correct?

A My understanding is again -- this calls for a legal conclusion, so my understanding as a layperson, is that that spot may not be enforced after the bankruptcy is declared. Yes, that is correct.

Q And so before the swap was terminated with Lehman, because it effectively was paying the floating rate --

A Uh-huh.

Q -- had an incentive not to have that floating rate go too high, or to hold the bonds itself, correct?

A Well, that assumes that it's going to be used strategically and is expected to go bankrupt. So I chose the 10th of September, so I think what you're implying here is that Lehman Brothers on the 10th of September says, we're going to go bankrupt, so let's be strategic here, we know that the fixed or floating slot was going to disappear, and let's take that into account.

Now whether they were contemplating bankruptcy at that time or not, I don't know. But if they were, let's just go back to August or July. They still had a liquidity crisis at that time, it was developing, and they certainly weren't, I don't believe, contemplating bankruptcy at that time. In which case, this scenario that you're, I think, trying to develop, I may be wrong, wouldn't apply, and so I can just make the point in July or August. It's the same point.

Q But the point is, unlike other auction rate securities holders, Lehman was not just an auction rate security holder, it was also the payer of the floating interest rate on the swaps. That made it somewhat different than all the other investors who held auction rate securities, correct?

A The slot made Lehman's position a little bit different because it had basically taken on some risk, in terms of paying this and the bond was a hedge. That is true. But if markets

are liquid, it could sell that bond, it could lay off that hedge, and solve its liquidity crisis. And I shouldn't say solve, that would not have solved the liquidity crisis certainly, but it would've moved in that direction.

Q All right. And because Lehman was somewhat different than the usual holder of offering of securities, it couldn't just sell that bond, without also dealing with the slot transaction, correct, pre-bankruptcy?

A I'm sorry, could you repeat the question again?

Q Sure. And because Lehman was somewhat different than the usual option rate securities investor, it could not just sell the bond without also dealing with the swap transaction, correct, pre-bankruptcy?

A Well, no, that's not true. It could certainly sell the bond. That would've raised cash. So let's break it down into the two parts.

By selling the bond, it would raise cash. There would be left with the risk of a fixed or floating swap. Now, it may not want to take that risk, although we certainly saw that Lehman Brothers was willing to take a fair amount of risk in other areas, but it may not have wanted to take that risk, but that doesn't preclude it from selling the bond, and either taking that risk, or laying that risk off in some other transaction.

Q Right. And if it was not able to lay off the swap, and it

had sold the bond, and the auction had failed, for all the reasons that you talked about yesterday about the turmoil in the market --

A Uh-huh.

Q -- Lehman would be faced with paying a twenty-two percent rate of interest, as a result of the failed auction, correct?

A So again, we’re talking about the turmoil in the market and why this is difficult. And --

Q Answer my question, please?

A I’m sorry?

Q Answer my question. It was a specific question.

And if it was not able to lay off the swap, and it had sold the bond, and the auction had failed for the reasons you talked about yesterday about the turmoil in the market, Lehman would be faced with paying a twenty-two percent rate of interest on the -- as a result of the failed auction, correct?

A So as I understand that hypothetical or the scenario that you’re laying out, Lehman has sold the bond, retained the fixed or floating swap position, and auctions had failed, so in that scenario, it would be receiving twenty-two percent --

Q That's right.

A -- it would be paying twenty-two percent or whatever the penalty rate would be, and it would be receiving 6.55, that is correct.

Q On the subject of auction rate securities, you don’t have

any extensive experience in trading or selling and buying auction rate securities, do you, sir?

A No, I do not.

Q Okay. And you are not a market participant, actually buying or selling auction rate securities during 2008, were you, sir?

A No, I'm not, and that's again, just to say it once again, why I didn't do my own analysis here, but I realize that I didn't have a feel for the market, and my judgment had a later date in the litigation concepts would not be appropriate.

Q And the market feel of someone who is actually in the market trading, buying and selling auction rate securities, you'd defer to that market feel, as opposed to substituting your own market feel for that person's judgment, correct?

A Basically what I've done is said that my judgment could not be based upon market feel, and so I understand what the market situation was, we had failed auctions, there was a lot of evidence in terms of pricing and volume out there that I can observe, but since I wasn't trading in the market, I didn't go to the point of figuring out what an appropriate mark would be for the Giant Stadium bonds.

Q Well, and in terms of the market turmoil, one of the observations you had yesterday is, there were in fact transactions that were taking place at par in the auction rate securities market, correct?

A My understanding, based upon everything that I've read and looked at is that most of those transactions that were occurring at par were what comes to be called forced buy backs where the issuer or someone involved is buying it back at par because of the failed auctions.

Q Right. And, in fact, that's a -- that's almost a feature of auction rate securities, that if you have a failed auction, the interest rate rises to such a high level, that the issuer is incentivized to buy back the bonds, because of the failed auction, correct?

A That can happen, yes.

Q And not can it happen, but you know from your reading, it was happening.

A It can happen, it was happening, it doesn't necessarily happen.

MR. TAMBE: Your Honor, now's a good time for a lunch break.

THE COURT: I think it's a fine idea. My question to you relates to your expected duration of further examination, only as that applies to when we come back for lunch. I'm wondering if we need a short lunch today or if a return at 2:00 o'clock will be sufficient. If the extra 15 minutes will help, we can come back at --

MR. TAMBE: I think 2:00 o'clock would be fine. I think -- I feel right now that I'm still on schedule for 3:30.

THE COURT: All right.

MR. TAMBE: Thank you.

THE COURT: We'll take a lunch break and return at 2:00.

(Recessed at 12:23 p.m.; reconvened at 2:07 p.m.)

THE COURT: Please be seated and please proceed.

MR. TAMBE: Thank you, Your Honor.

BY MR. TAMBE:

Q Good afternoon, Professor Pfleiderer.

A Good afternoon.

Q Let's turn to a different topic than the one we were discussing before lunch and this is the municipals and the valuation of municipals. And I believe in slide 71 through 73 of your demonstrative's binder, you have a few slides prepared about municipals, correct?

A I believe it may be those numbers, yes.

Q Okay.

MR. TAMBE: If you'd pull up BCI Exhibit 1103, slide 71.

Q And what you're showing here is the total amount of securities, municipal securities that were acquired by Barclays and you've divided them up into level one, level two, and unavailable, correct?

A That is correct.

Q And the next slide, 72, you kind of split that out between

auction rate and non-auction rate securities, correct?
A That is correct.
Q And we've discussed the auction rate securities, but with respect to non-auction rate securities, you see that differential in value, the last two columns, Barclays' exit value 922 versus movant's exit value 919.
You'd agree with me that the vast majority of that differential is a result of a mistake by Barclays, correct?
A The -- I agree there were seven bonds that were marked by BoNY at, I think it was seven, but I think a hundredth of a cent, and that was carried over. That was a mistake, yes.
Q Okay. And if you'd turn to the next slide, slide 73, you have those bonds listed. You have them as eight municipal bonds Barclays adopted the BoNY marks one-tenth of one penny, a hundred percent at level two. Do you see that?
A That's correct.
Q You don't have any indication on that slide acknowledging that this was a mistake.
A That was a mistake, yes.
Q Okay. And it was a mistake for you not to note that on the slide, wasn't it, sir?
A I don't know that that was a mistake, but it certainly was a mistake that was made apparently by BoNY and then carried over through into the acquisition balance sheet, yes.
Q Right. But along the way and we've been through this

process that you say it's a mistake made by BoNY picked up PCG and audited by PwC, reviewed by Professor Pfleiderer, and no one picked up this mistake, correct?

A That is correct.

Q That's about a hundred million dollar mistake?

A I don't believe it's that large, but I'd have to go back. I believe it's like more seventy-eight, eighty million, but I'd have to check. My recollection is not perfect here.

Q What was the materiality threshold set by PwC for errors in adjustments on a category-by-category basis, sir?

A I don't actually recall precisely.

Q Could it have been as much as five million, ten million, twenty million dollars per category?

A I'd have to go back and check what they had per category.

Q That's not something you looked at when you were reviewing the PwC's work papers, in terms of where they drew the line on materiality?

A It was such something I certainly was aware of at the time, but I can't recall right now.

Q Now, you have seen Mr. Teague's testimony with respect to these bonds that were priced at one-tenth of one penny, correct?

A I believe I have, although I can't -- I'm not remembering the specifics of it right now.

MR. TAMBE: Can we just pull up that testimony? It's

the Teague deposition testimony at page 167. It'll just come up on the screen in a second.

(Pause)

MR. TAMBE: If you'd highlight from lines 5 down to line 13, please, and enlarge.

Q And what was Mr. Teague was asked, I'm sorry, what was an oversight, pricing of one-tenth of one penny was an oversight. Answer, yes, I believe there was an oversight on our part. We had no data to mark those assets.

What have you done to correct that oversight? The oversight itself was brought up after the opening balance sheet was closed.

Is it the case, sir, that Barclays had no data to price those securities, where it chose to take BoNY's one-tenth of one penny price?

A I'd have to go back and review exactly what was the case for these seven or eight bonds, but generally speaking, and I don't know if it applies to this case, but I believe taking his testimony as given here it does, that in those cases where Barclays was not able to come up data -- that from other sources it did revert on occasion at least to the BoNY marks, yes.

Q But it didn't do so when there were FTID prices available, correct, the Financial Times Interactive Data process?

A I believe that the intention was that when they were

outside vendor prices or some prices that were available to use those and not rely on the BoNY marks generally speaking, yes.
Q In fact, you note on your slide 73 --
MR. TAMBE: If you could go there, please.
Q -- the second category the 486 non-ERS municipal bonds, in fact, you have a bullet that says, FTID prices used. Do you see that?
A That’s correct.
Q And do you know one way or the other, sir, these seven bonds where Barclays took the one-tenth of one penny price and Mr. Teague said there was no data available, were FTID prices available and provided for in Barclays’ own spreadsheets for those securities?
A I don’t recall. I’d have to go back and check.
Q That’s not something you looked into?
A It may be that I did at the time but I don’t recall sitting here now.
Q Now, let’s talk about the non -- some of the ARS portion of the municipal portfolio. And going back to your slide 72, and you’ll see there’s a differential between the Barclays’ exit value and the movant’s exit value for the valuation of the auction bid securities in the municipal bucket, correct?
A That is correct.
Q And then that’s primarily driven, if not exclusively driven by the fact that what Barclays did was take the quoted

prices and reduced them by twenty percent, a twenty percent liquidity discount, correct?

A It applied a twenty liquidity discount, yes, that's correct.

Q And movant's expert, Mr. Schwaba priced those at par.

A That is correct, I believe, yes.

Q Do you have any basis, sir, to opine on whether a twenty percent adjustment for auction rate securities in the municipal space was reasonable or unreasonable?

A Well, again, we get into the philosophical problem that we've got a market that basically is almost completely closed down, and for which there are very few trades. So when we don't observe many trades, they're trying to construct what an exit price would be, and we know that it's an illiquid market where you don't have liquidity, and so the determination was made here to reflect that illiquidity by taking a twenty percent discount, and if I recall, PwC reviewed that and found that reasonable.

Again, it's hardly a manner of judgment here, based upon trying to assess what the situation in the market is at the time, and what's a reasonable adjustment to take, given that there's very little liquidity in the market.

Q Right. And the question for you, Professor Pfleiderer, was do you have an opinion or basis to judge the reasonableness of that judgment call that was made by others?

A I mean, in the sense of do I have an opinion based upon having a feel for the market, no, I wasn’t there. I know a fair amount about the market conditions at the time. Volume had fallen off tremendously since the beginning of February in these bonds, and so the question is, as I said one of judgment of determining what is a reasonable exit mark, given that you have a market that’s, for all intents and purposes, virtually closed down.

And so I guess I'll use the language of pre-PwC, based upon my knowledge, I certainly don’t find this unreasonable. And I think it was a reasonable judgment that given the market that had broken down, one would take a substantial liquidity adjustment.

So I think that taking the liquidity adjustment to the significant margin is much more appropriate than pricing it at par.

Q And you believe the twenty percent liquidity adjustment was a significant adjustment, correct?

A It’s certainly not trivial, yes.

Q How about a thirty percent liquidity adjustment, would that have been substantial and significant?

A It would’ve been greater than twenty, yes.

Q And -- I know that. But in your view, would that have been a reasonable adjustment to take with respect to municipal auction rate securities?

A Well, at some point, as we go down this path, we start to approach unreasonableness, and again, it's a matter of having a feel for the market, and it's again, a philosophical problem when there's really very little and no ability to trade in a market because it's broken down. How do you reflect that in an exit mark? And I think that twenty percent discount is certainly a reasonable reflection of the fact that the market is broken down and there's very little liquidity.
Q How about a ninety percent discount? Would that be reasonable in your estimation?
A I think for my purposes, that would -- depending upon the market, depending upon the circumstances, and depending what you're attempting to do, that would perhaps approach a level of unreasonableness in certain circumstances. But you need to basically describe exactly what those circumstances are.
Q And in terms of describing those circumstances, did you attempt to do that with respect to any of the auction rate securities? Did you try and look at the securities, the credit characteristics, the issuer, to determine whether a flat twenty percent or thirty percent discount was appropriate or some other adjustment was more appropriate?
A So --
Q Did you attempt to do that is the question.
A I looked at the market conditions at the time, and I looked at the type of ARS securities that they had, and I

didn't do a full scale analysis, because again, I didn't have a feel for the markets at the time, but it struck me as being reasonable to take something on the order of this magnitude.

Q Well, on the Giants' auction rate securities, what Barclays took for three of the four, was a ninety percent adjustment. They valued them at ten cents on the dollar. That's not reasonable, is it, sir?

A Well, the Giants are obviously different, because that's not a municipal that is issued by a corporation, the Giants, and so there are differences there. And it's difficult to figure out how those factor in to get a precise number, but I would certainly say that it's reasonable to take a substantial discount from par, given that these were bonds that weren't trading and they failed at auction.

Q So as I understand your answer then, taking a ninety percent discount on three of the four Giant Stadium bonds, it is not your opinion that that's reasonable, is it, sir?

A I would think that that is closer to the unreasonableness threshold, but the valuation at par is very far from reasonableness, so we don't know quite where it is within this range that's reasonable, because there really is a range. But I can't say we're farther away from what's reasonable when we value them at par, then when we take a substantial discount.

Q Well, there lots of factors that would go into where in that continuum you fall, correct?

A That is right, and that's where we -- where you come to a manner of judgment in that case.
Q A manner of judgment and market feel, correct?
A That is correct.
Q And would depend on, for example, the credit rating of the issuer, correct?
A That would be one consideration but it wouldn't be the only one.
Q It would depend on considerations such as what is the maximum rate in the event of failed auction, correct?
A That would be another consideration.
Q Because you and I have discussed before that that max rate can incentivize an issuer to redeem bonds, correct?
A That is correct.
Q And closing the circle on the auction rate securities, it seems to me that you find yourself in a position where you are prepared to second-guess a par valuation, but you are perfectly comfortable with a twenty percent discount off of par; is that right, sir?
A With a twenty percent?
Q Yes.
A I'm much more comfortable with a twenty percent than what I am basically pricing at par. So my knowledge as a financial economist and the breakdown of this market would say that par is definitely unreasonable.

If you ask me is fifteen percent, eighteen percent, or twenty-three percent more reasonable than the other two, that I really am not prepared to opine upon because I didn't have a feel for the market, and this is a range where reasonable people can disagree. But pricing it at par, I mean, there's very little liquidity in the market when you're instructed to price it at an exit mark, basically you're instructed to price it for what you could sell it at, I think that that is unreasonable.

Q Okay. And you do know, do you not, sir, that Barclays priced for auction rate securities at par?

A I'm sorry?

Q You do know, do you not, sir, that Barclays priced for auction securities, auction rate securities at par?

A I believe they may have done that, yes.

Q But that would've been unreasonable?

A That would've been, in my view, depending upon the securities, that could very well be unreasonable if there was no market for those securities.

Q And again, you didn't do any such analysis when you were looking at this portfolio of auction rate securities to determine whether in a particular instance when Barclays used par, whether that reasonable or unreasonable, correct?

A I was looking at the overall process and the assumptions that have been made to value this group of securities, and so

taking a twenty percent discount, based upon the substantial illiquidity in the market, and the fact that these auctions had failed was, from my opinion, within the bounds of reasonableness.

Again, I can't quantify it, and I'm not going to sit here and say that it would've been more reasonable if it was twenty-three or more reasonable if it was seventeen, but what I can say with substantial confidence, is that pricing it at par would've basically been not taking into account the market conditions at the time, that can be easily seen by just looking at the fact that this market had basically failed.

Q But again, you'd agree with me that someone who was actually transacting in the market, has familiarity of the market, may have a slightly better street sense of that market, than for example, someone like you?

A I would agree with that, yes.

Q Let's move to Pine, please, and that is -- you had a discussion of Pine on pages 43 to 50 of your demonstrative. There was one place, in particular, that I want to draw your attention and that is slide 45 of your demonstrative, BCI 1103.

And before I delve into this analysis, you did not do any independent round-up analysis of the Pine valuation, correct?

A That is correct.

Q For example, you didn't go to LoanX or CES spreads to determine the probability of default of any of the borrowers,

correct?
A No, I did not.
Q And you didn't have your staff do that either, correct?
A No, I did not. I did not -- I should say, I did not instruct my staff to do that.
Q Okay. So -- and again, in this instance, you saw a valuation in the first instance that was done by Barclays, the PCG Group and then reviewed by PwC, and then you reviewed what PwC had reviewed, and you reviewed what Barclays had done, correct?
A Among other things. I was looking, as you can see, at some other valuations, including the valuation that JPMorgan made, and Gifford Fong who I can tell you is far more qualified than I am to make these valuations. He does that as a business.
Q You know, I noticed that on your slide, you have a date for JPM, when you say, on September 12th, JPM revalues at seventy percent. Do you see that?
A Yes.
Q Yeah. But you have no date next to the Gifford Fong valuation. Do you know when the Gifford Fong valuation was rendered?
A I believe it was before that or at that time. It's certainly, if I recall correctly, and I'd have to go back and look, I believe it's mentioned as something that had been done

before, certainly before the bankruptcy. I know it's been done before the bankruptcy.

Q Well, let's not guess about it. Let's pull up, if we could please, BCI Exhibit 1005. I think that's the document you were shown yesterday.

(Pause)

MR. TAMBE: We may not have it in our system, it's a relatively new exhibit. Thank you. If you could please pull it up.

UNIDENTIFIED SPEAKER: 1005?

(Pause)

Q That's the e-mail you were asked about yesterday, correct, sir?

A Yes, it is, I believe.

Q That has a date of September 4th, 2008, correct?

A So, yes, it is, at least a couple of weeks before the bankruptcy.

Q Right. And some fairly tumultuous weeks between September 4th and the bankruptcy, correct?

A Those were weeks of some turmoil, yes.

Q So on September 4, 2008, Gifford Fong comes out with a fifty percent valuation. Now, let's go back to your slide, slide 47.

A Excuse me, I don't want to interrupt, but I'm not sure when Gifford Fong came up with the valuation, this is an e-mail

reporting it on September 4th.
Q This could be an e-mail --
A We don't know when Gifford Fong actually made that valuation, but it was presumably before September 4.
Q That's a very good point. So at least September 4th or earlier, you got the Gifford Fong valuation.
MR. TAMBE: Go back to slide 45, BCI 1103.
Q And at least eight days later as the prices is worsening, JPM, you say then revalues Pine at seventy percent.
A That's correct.
Q So they've got a different view from Gifford Fong, and in fact, they ascribe a higher value to Pine.
A Yes. And this is yet further evidence of how a security like this, which Barclays classified as being a level three security, when it was classified by Lehman as level two, is extremely difficult to value, and it requires some judgment, which was the point I was making yesterday, and I think this illustrates it as well.
Q And you see this as an exercise by JPM as an independent judgment, they got some information from Gifford Fong, but they independently value it at a higher value, correct?
A I'm not sure whether their valuation was made taking into account Gifford Fong's valuation, or whether it was made not taking it into account and made independently. All I know is Gifford Fong valued it around fifty percent. I think it was

Mr. Delaney at JPM valued it at seventy.
Q And when you say JPM valued it at seventy, is there a document you have in mind where you actually saw JPM valuing this at seventy percent?
A Well, I certainly saw it in the examiner's report.
Q So you saw a reference to it in the examiner's report. Did you see any underlying documents from JPM that show JPM valuing this at seventy percent?
A If I did, I'm not recalling it as I sit here, but I may have, but I do remember it in the examiner's report.
Q Did you see any documents where JPMorgan valued this at a hundred percent after September 12?
A I don't know what the custodial mark was, but I believe it might have been -- I'd have to go back and check. I think there may have been a custodial mark at a higher level, I'm just not sure.
Q Well, let's check the custodial mark. Let's go to M-909.
MR. TAMBE: We'll pull that up on the screen, it's Movant's Trial Exhibit 909.
Q And there's an Excel spreadsheet. First, let's look at the e-mail. Do you see there's an e-mail on 9/26, so post closing from Stephanie Heller at the Fed to Mr. Laraca at Barclays Capital. Do you see that?
A I do, yes.
Q Copying Stephen Cutler and Tom Baxter at the Fed.

A Right.

Q Steve Cutler at JPMorgan and Tom Baxter at the Feds, yeah.

A Yes. I don't know who those two people are, but I'll take it that they're JPMorgan and the Fed, yes.

Q And what's being sent over is here's a list of securities pledged to the Fed Wednesday to Thursday. Do you see that?

A I do, yes.

Q And you recognize that as a reference to the week of the 15th, the securities that were pledged to the Fed, Wednesday into Thursday.

A I believe that must be what it's referring to, yes.

Q And then the file has a name 080917 next to that, do you see that column?

A That would certainly indicate that it's a point at that timetable.

Q Let's take a look at the value of the Pine security in that Excel spreadsheet.

MR. TAMBE: It's a PDCF tab, please. Ought to be the very first one, and then we just need to expand it. Expand row -- column F, please.

Q Do you see the CUSIP that appears there in row F -- in column F, row two?

A Yes. I recognize the AA7 as referring to -- I can't say it refers to Pine, but I know that the Pine CUSIP ended with AA7.

Q Right.

MR. TAMBE: And if you'd scroll across, please, Steve, slowly. Stop. You see the -- I have trouble seeing it now.

Q You see the price column has an M -- in column M, 2 is 100. Do you see that?

A I do, yes.

Q And you see the market column, column J-2 has a value, lots of numbers in there that's about 919 million. Do you see that?

A I do.

Q Okay. And you have no reason to doubt that this is, in fact, JPMorgan's custodial value on the Pine security on September 17, 2008, do you?

A No. I take it as that was the value, and what that indicates to me is how unreliable or potentially unreliable some of these custodial marks are. In particular, here we have the JPMorgan as custodian placing the price at a hundred, when I understand from the examiner's report, that internally it was valuing it at seventy, and Gifford Fong had valued it at fifty.

So I think that just illustrates the type of thing that we're talking about here, where taking an inventory in at custodial marks is not necessarily going to be reliable.

Q Well, you are not an expert on custodial customs and practices, are you, sir?

A No, I'm not representing myself as such, no.

Q And you are aware, though, as a financial economist, that large institutions like JPMorgan have some processes and procedures in place when they're asked to do important things, like serve as custodial agents, correct?

A I know, but it -- I'm aware of that, but what we have before us is a situation where internally JPMorgan was valuing it at probably in one part of its institution at seventy or seventy-four, I think it was, getting a report from Gifford Fong, who is an expert in this business, valuing it at fifty-four, fifty something, and then they're putting a price of a hundred on it here, a little bit later in a very tumultuous period.

So I think as a financial economist, I may not be an expert in custodial practices, but I do believe I have the expertise to realize that this calls into serious question that price of a hundred there, when in other parts of the institution, they're marking it at a much lower price.

Q Well, the reality is, you don't know what JPM may be marking it at in different parts of the institution, you're speculating as to that?

A I'm --

Q Based on the examiner's report.

A By reading the examiner's report. My information, I believe, is mainly from the examiner's report, that is correct.

Q And earlier today we discussed the definition of market

value in the e-mail that was shared between Ms. Leventhal and Jonathan Hughes, correct, and that was the definition of market value as it relates to the PDCF. Do you remember that discussion?
A I do remember, but I want to be careful here. That was market value as what -- I should have to have my memory refreshed, as to exactly what that context was, and whether it was market value for purposes of posting values for the repo or market value as an economist would understand it.
Q So you may have a completely different view of market value than the definition ascribed to by the Fed and JPM as set out in their contracts; is that what you're saying?
A I'd like to go back and review what that was, just so that I can review it and make sure that if I'm answering your question, I'm answering it as I would as a financial economist.
Q Well, let's look at M-705. That was the e-mail that we were looking at this morning. Page two of M-705.
MR. TAMBE: And if you could increase the size of that, please.
Q And what Shari Leventhal is saying to Mr. Hughes at Barclays is, this is the definition of market value used in the PDCF program. You understand that to be the Fed program, correct?
A That's the Primary Dealers Credit Facility, yes. So here we have a problem right away. This is why I wanted it put back

up on the screen, because I was remembering something like this. If you read that, it says, market value, the most recently available closing bid price for the particular security.

Well, this is a security that never traded. We're talking about Pine, it never traded. There's no bid price that's out there. So here's where someone has to use judgment, and you have Gifford Fong, you have internally and JPMorgan, at least according to the examiner, you have a price, and then you have the custodian putting a price at hundred is not the most recently available closing bid price for the particular security.

So I, with all due respect, I don't think that this definition can be applied in this situation where you have a security that was not traded and was never meant to trade.

Q You haven't seen any communications between JPMorgan and the Fed where JPMorgan says, we know you've got a definition of market value, but we're going to disregard that for the following classes of securities. You haven't seen anything like that, have you, sir?

A Not to my knowledge, but this definition that you've put up in front of me, I don't think can be applied to Pine.

Q Let's move to US Agency securities. In your demonstrative, you had slide 66 and others where you discuss some of the valuation issues concerning agency securities,

correct?
A That is correct, yes.
Q And you see there that there is a differential in value between the movants' exit values and the Barclays' exit values. Do you see that?
A That is correct.
Q And you understand from work you've done in this case, that part of that relates to price differential, but part of that also relates to a liquidity discount differential.
A That is correct.
Q And just so we can put some definition around that, if we could turn to a demonstrative we used earlier with Mr. Slattery just to talk about the differential on Movant's Exhibit 920, page 7.
MR. TAMBE: The next page.
Q All right. And here what Mr. Slattery has done is just divided up the differential amongst different types of U.S. treasuries and agencies, and you'll see that the bulk of the differential in price and value comes from U.S. agency debt securities, and most of that difference comes from liquidity adjustment. Do you see that?
A Yes, I do.
Q Okay. And that's consistent with your review and analysis of his work, correct? That's where the differential comes from.

A Yes, I would agree with that.
Q Okay. So now let's go back to your slide then.
What work did you do to satisfy yourself that a five percent mid-to-bid adjustment, so a ten percent bid-ask spread was appropriate for those particular CUSIPs?
A So again, I'm relying here on the traders and the people that are close to the market and knew what market conditions are. Again, if you look at this, what you see is that level two securities and we're in that middle part of the spectrum make up a substantial part of this portfolio, and these are the ones that are more difficult to value, and for which price information is harder to come by, and have a lower liquidity.
So those that were in the market at Barclays, and this is again reviewed by PwC, are making a judgment as to what the liquidity adjustment should be. I was not in the market, and so I didn't have the feel for the market to make a judgment against that.
Q Did you look at any publicly available data, any published data about what prevailing spreads are in this market?
A Well, you can see prevailing spreads on some of the more liquid securities, and so-called benchmark securities, and by definition, those are going to be lower. So that information is not going to tell you how to basically make the liquidity adjustment to this overall inventory.
Q Well, did you make any effort to determine how, if at all,

the traders at Barclays had gone from the benchmark securities to liquid securities to this five percent, this ten percent bid-ask spread that they apply here?

A No, I did not make any effort to do that.

(Pause)

Q And do you have any greater level of specificity as to your knowledge how that five percent was arrived at? You said you got it from traders. How was that five percent arrived at?

A No, I didn't say I got it from traders, but it was, I believe, formed by those that were in the market, again, had this feel for the market at the time, but I don't know precisely how the information for that was gathered.

Q Are there any names of the PCG Group that you associated with that decision to have a ten percent bid-ask spread on US agencies?

A There may be, but I don't recall at this time who was involved.

Q And you don't recall seeing any work papers that -- specifically Barclays' work papers, specifically lay out the rationale, the analysis for that five percent adjustment?

A Not that I can recall sitting here.

Q And you'd agree with me that that five percent drives a non-immaterial differential between movants and Barclays, 370 million dollars, correct?

A It was a number that I think we saw up there, at least I

believe that's an order of magnitude -- as an order of magnitude, it's fair in terms of representing the difference.

Q You have seen some of the materials that Mr. Slattery has put in about publicly available information, Fannie and Freddie publication that actually reported on what the prevailing spreads were in September 2008 for agency securities, correct?

A Yes, I did.

Q And that shows spreads that were, I think, bid-ask spreads and liquidity adjustments of about two basis points; is that right?

A I believe those were for the most actively traded benchmark bonds, yes.

Q So let's just to be sure that we're looking at the right information, we can go back to Movant's 920, slide number nine, which is page ten, I believe.

You've seen this before, right?

A Yes, I have.

Q And the Fannie Mae spread of .02 percent, that's consistent with what you saw in the materials cited by Mr. Slattery, correct?

A I think that's -- yes.

Q And what Barclays has applied, the 5.8 and the 4.8 percent is several hundred times the spread experienced on the Fannie Mae securities, correct?

A Those Fannie Mae securities again, I believe, are the

benchmark securities that tend to be very actively traded, yes.

Q And you did not do any further analysis to determine the appropriateness of using that wide a spread across all of this class of securities?

A No, I did not.

Q Okay. Let's move to agency RMBS. And in your demonstrative, that's slides 80 and 81, so let's move to slide 80 and BCI 1103.

And here again, as you've done on other instances, you're describing the level one, level two, level three status and the differential in values. Do you see that?

A That is correct.

Q And on the next page, page 81, you lay out some methodology, correct?

A That is correct.

Q And the second bullet or well the first two bullets talk about the use of a model. Do you see that?

A Yes, I do.

Q And you referred to that model in the second bullet point as the Black Rock prepayment model. Do you see that?

A Yes.

Q Did you actually examine the model that was used by Barclays to come up with these valuations on this class of securities?

A In this particular case, I did not, no.

Q And the model would have a series of assumptions and inputs that would drive an output, correct?
A That's true of any model.
Q And you did not examine the inputs and assumptions that went into the Black Rock prepayment model used by Barclays to arrive at the prices that they arrived at for these securities, correct?
A I did not, no.
Q Okay. And you did not create your own model to try and replicate -- test what Barclays had arrived at, correct?
A No, I did not.
Q It sounds from your last answer, the Black Rock prepayment model is something you're familiar with, correct?
A I'm familiar in broad-brush strokes, but I haven't used it and I don't know the details.
Q So you've never used it?
A I've never used it, no.
Q Are you familiar with other prepayment models other than the Black Rock model that are used in the industry?
A I'm familiar with how the models are generally used, but I'm not that familiar with all the specifics.
Q And with respect to the models that we used by movant's experts, did you try and analyze those models?
A No, I did not.
Q And did you -- but you did try to analyze a lot of the

inputs and assumptions used by Mr. Slattery in arriving at his numbers, correct?

A Some of those I did, yes.

Q And you took -- you told us about you and your staff having spent countless hours trying to figure out how Mr. Slattery arrived at a particular number, right?

A That was a different exercise. It wasn't looking at his actual inputs in terms of assumptions of CPRs and weighted average life and things of that sort. It was rather and a simpler exercise than that, which was simply to try to identify where in his work papers he had calculated midpoint or mid-level prices.

Q And you're not suggesting that we hadn't provided you with the assumptions that were driving this model. You were looking for a particular piece of information that you couldn't find in the work papers, right?

A What my staff looked for and did not find was a situation for a number of the CUSIPs where a mid price had been calculated, based on whatever inputs he had, that filtered up into the spreadsheet, which I'll characterize as a top level spreadsheet, as a midpoint price range from which a liquidity adjustment was taken.

Rather, what we found was the output of models that he was using, filtered up as a bid price, or appeared to. I'm going to say appears to. A bid price, which was then, it appears,

grossed up to mid price.

Q And you don't quarrel with the notion that you could have models that, in fact, because they're driven by market inputs generate a bid price as opposed to a mid price, correct?

A In principle that could be done, but the practice, as far as I understand it, is always to generate mid prices and scale them down. And my understanding was that Mr. Slattery represented, at least in some of his testimony, that he was generating mids and then adjusting them down to bids. So it was based upon that that we attempted to look for where the mids were generated in his underlying work papers.

Q Did you spend the same time of effort and ask your staff to turn over every stone looking for assumptions and inputs and drivers of the Barclays' model, sir?

A This exercise obviously required some effort. We did not do that effort throughout what Barclays was doing, in some sense, that was done by PwC.

Q Well, you don't know to what extent PwC did -- conducted that effort, do you, sir?

A That's why I qualified it by saying in some sense. I know that PwC, if you look at their work papers, did extensive testing. As a matter of fact, I pointed out yesterday to a case where they were looking at exactly this type of situation where a matrix pricing was used, and they looked and they saw that the wrong matrix was being used, so they were looking very

carefully at the process, at least in that case they certainly were, because they identified an incorrect matrix being used.

Q And other than that case that you talked about yesterday, you can't comment on how carefully or how appropriately they may have looked at and studied the model used by Barclays to arrive at these values, correct?

A No, that's not correct. I looked through their work papers, and I saw instances where they were doing lots of analysis to examine whether the pricing that was being done by Barclays was using the same process and the same models as was being used for their legacy portfolio. I had a number of issues in mind where PwC was basically doing these type of checks.

I don't think that PwC checked everything. It take -- it took representative samples, it looked at the process, but it was a very extensive procedure of basically doing this type of analysis.

Q Do you know whether PwC in all the work that it did, obtained the risk premium inputs that were used by Barclays to run their models?

A Sitting here now, I don't know. I'd have to go back to their work papers. I believe that they did send outside checks. I believe -- actually, I'm pretty sure. Let me say I'm ninety percent confident that the following occurred, that for various types of securities, they got -- they used this

group, and I can't remember the acronym as I sit here now, on this internal to PwC to basically use their own models to see if the prices that they came up with were similar.

So I think that the exercise was not looking specifically at whether the inputs into the Barclays' model were what PwC thought they should be, although that may have been done as well. But rather, to look at the Barclays' prices, send those prices to this group within PwC and have that group use its own models to see if they came up with similar prices.

So I'm quite confident. We economists always like to quantify these things in some way. So I'm ninety percent confident that they did that in at least the one case that I'm thinking of, and I think in other cases as well.

Q Going back to your slide, you say that in addition to whatever models and assumptions were used to drive the pricing methodology, which was run by Barclays, and in your view, tested in some way by PwC, there was also a liquidity discount taken for the prices that were then obtained, correct?

A That is correct. So they had obtained what we would call mid value prices or midpoint prices, and then mark them to exit values as required by the accounting rules.

Q And for the agency CMOs, you see there that there was a ten percent liquidity adjustment taken by Barclays, correct?

A That is correct.

Q And you understand that to be a twenty percent bid-ask

spread, right?
A Well, that is an adjustment that was marketing their mid values down to a bid value. I'm not sure in some of these cases whether they're interpreting it as half of a larger spread, or whether part of it is an adjustment to value to reflect market conditions, so.
Q You just don't know?
A I don't know in this case exactly what the interpretation was.
Q And you have no street sense, knowledge, about whether ten percent mid-to-bid adjustment for agency CMOs was appropriate for all of the different types of agency CMOs that were at issue in this case, correct?
A If by street sense you mean did I have a feel for the market --
Q Yeah.
A -- that phrase that we've been using for, no, I was not in the market at the time, and so I don't have that street sense or feel for the market.
Q And you do understand, though, that in this market, the agency CMO market, there are many different flavors or stripes of products that are traded, correct?
A There's a very large, a very extensive range of IOs and POs and varied sequentials and various other things, yes.
Q And you do know that liquidity and bid-ask spreads would

vary from product-to-product within this segment, correct?
A That would generally be the case, yes. And here again, you're taking an average over a range of products, so there's a certain level of granularity that they decided to do and they basically lumped the CMO products together and took what they thought was an average over that.
Q And again, this is an area where you would defer to someone who actually had that sense of the market, who actually had traded in value these types of securities to determine what an appropriate bid-ask spread should be for particular subcategories of the segment, correct?
A Indeed. I would say that someone who is there in the market at the time, or has the sense of the market at the time would have more information to do this than what I would.

MR. TAMBE: If we can take about a five-minute break, Your Honor. I think I'm almost done. I may have two areas to cover, but I just want to make sure I don't have anything else left.

THE COURT: Fine. We'll take a five-minute break.

(Recessed at 2:55 p.m.; reconvened at 3:14 p.m.)

THE COURT: Be seated, please.

MR. TAMBE: Your Honor, we let counsel know at the break that we have no further questions on cross. Thank you, Professor Pfleiderer.

THE COURT: Okay.

MR. HUME: Short redirect, Your Honor.

THE COURT: Okay.

MR. HUME: For the record, Hamish Hume, Boies Schiller, representing Barclays.

REDIRECT EXAMINATION

BY MR. HUME:

Q Good afternoon, Professor Pfleiderer.

A Good afternoon.

Q I have just a few questions in follow-up to Mr. Tambe's questions.

On two different occasions I think in his cross-examination, Mr. Tambe showed you Movant's Exhibit 190, an e-mail attaching a spreadsheet. Do you recall that?

A I believe so, yes.

Q And do you recall that this was in response to the analysis presented in your report in January of this year, as well as supplemental information you provided, showing that the Lehman book value of the long positions, as defined in the APA, were never higher than seven billion dollars during the week of September 15th.

In response to that, Mr. Tambe has shown you this spreadsheet. Do you recall that?

A Yes, I do.

Q And we have the spreadsheet now up on the screen, and you don't recall studying this spreadsheet in close detail, do you?

A Not in close detail. I believe I've seen -- maybe not this one, but something similar, but I certainly didn't study it in very close detail.
Q It has on that an entry for a number of CUSIPs, including one CUSIP here, Bank of Obio (ph), Argentina, it looks like. Do you see that, the description?
A Yes, I do.
Q And you see in column H it has a quantity of 257 million?
A Yes, I do.
Q And you recall Mr. Tambe representing to you that if you totaled up all the market values, it may be in excess of seventy-three billion.
A Yes, I do remember him saying that, yes.
Q Suggesting that that might be inconsistent with all of your findings that you set forth over the past year, that there's no data showing long positions as defined in the APA greater than seventy billion Do you recall that?
A I do, yes.
Q Do you see the market value column K?
A I do, yes.
Q Do you see for this one single CUSIP, there is a market value of 28.2 billion dollars.
A That does get one's attention, yes.
Q In all of your analysis, the long positions, and the APA, the GFS data, and the CUSIPs transferred to Barclays, have you

ever heard of a single bond with a value of 28.2 billion dollars?

A No. I believe that would've been something I would've remembered, yes.

Q Is that inconsistent with your understanding of what was actually in the collateral transferred to Barclays?

A It's not at all consistent with what I believed was transferred. I certainly think if it would've been transferred we would've been talking about it if it had that market value.

Q Does it strike you as likely that there even was a single bond from Bank of Obio for 28.2 billion dollars?

A No. My suspicion would be that that is some sort of clerical error or a calculational error. That would be a huge bond.

Q And if there were a single bond in this list of 28.2 billion, what significance would there be to you that the total spreadsheet adds up to somewhere like seventy-three billion as Mr. Tambe suggested?

A That would be certainly sufficient to put it over seventy billion, certainly would get it to seventy-three billion; twenty-eight billion would certainly fill that gap, yes.

Q And if the 28.2 is included in the calculation that leads to the seventy-three, would the seventy-three have any significance or impact or cause you in any way to modify any of your opinions in this case?

A Not at all, unless I understood that that bond really did have that value, and was defined as part of the loan positions, but I certainly haven't seen anything to indicate that that would be the case.

Q We have prepared a demonstrative to, for efficiency sake, so as not to have to go through a series of documents, or if movant's counsel insists, I'm sure we could, showing the valuations that are given for this Bank of Obio bond.

If that's the CUSIP number, it's a Obio bond. First we have Movant's 190N, which we just looked at and summarized. Do you see the 28.2 billion dollar number there right here?

A Yes, I do.

Q Okay. Underneath that, we have taken the BoNY midpoint value, given for the same bond. You see it has the same quantity, 257,500,000?

A Yes.

Q It's exactly the same with BoNY. Do you see that?

A It's precisely the same, yes.

Q And the price is precisely the same.

A Indeed.

Q You see the market value is quite a bit different.

A It looks like it's reduced by a factor of a hundred here.

Q And this --

A Approximately.

Q -- I represent to you, Professor Pfleiderer, is taken

straight off of Movant's 285N, the rates tab. Can you think of a reason, Professor Pfleiderer, why the BoNY value would be one hundred times less than the value of Movant's 190N?

A I can speculate that perhaps, this is just speculation, that somehow cents were put in instead of a dollar, given that it looks like a factor of a hundred difference, that might be the reason. I'm just not sure.

Q Can you see from the numbers that it is exactly, or it appears to be almost exactly a hundred times different?

A Yes.

Q Now, the Barclays' mid value taken from Movant's 285N is 271 million. Do you see that?

A Yes.

Q And the movant's expert has an exit value of 260.2 million. Do you see that?

A I do.

MR. HUME: And I want to be very careful, Judge, not to be representing here that Barclays' actual value on the acquisition balance sheet was higher than movant's expert, Mr. Olvany, just for simplicity, it was easier for us to take the mid value that Barclays calculated, so that we could list every number exactly as it is on the spreadsheet and keep everything apples-to-apples. I think that Barclays' exit value is lower, I believe, or I would guess, than Mr. Olvany's.

Q And then finally -- so you see Mr. Olvany's value,

Professor Pfleiderer?
A Yes, I do.
Q And is it in -- is it comparable on the same order of magnitude to what is on Movant's 190N?
A It is. Oh, wait, I'm sorry. The top line is not at all. It's again, different by a magnitude of ten to two, a factor of a hundred.
Q And finally we have, do you see the GFS data extracted from September 19th with a value of 259 million. Do you see that?
A I do.
Q How does that compare to what's on Movant's 190N?
A Again, in the same order of magnitude. Oh, wait, I'm sorry. To 190N, it's again a factor of a hundred, but it's the same order of magnitude of all the other lines.
Q And how does this information impact your assessment of the relevant, if any, of the information on Movant's 190N that is presented to you today in response to all of your findings over the past year?
A Well, my strong speculation and I'm fairly confident in making this statement, is that Movant's 190N is plagued by a substantial calculational error of some sort that puts that value off by a factor of a hundred and makes it unreliable.
Q You were also asked some questions about the testimony of the people who were involved in negotiations at the time. You

were shown testimony from Mr. Lowett. Do you recall that?
A Yes, I do.
Q And I think you gave some testimony that in terms of what was actually negotiated, you would defer to the people who were actually there at the time. Do you recall that?
A Yes, I certainly would.
Q Are you aware, Professor Pfleiderer, of the trial testimony from Mr. Lowett and Mr. McDade regarding whether it would be better for the Court in its search for the truth about the Lehman marks, to rely upon their recollection rather than to rely upon the actual data from the Lehman systems?
A I do recall that both of them said that it'd be more reliable, if not in this precise way, but basically saying it would be more reliable to go back and look at the books rather than what they were remembering. Again, I'm characterizing what they said, but I believe that both of them said that.
MR. HUME: Could we have the trial, the official trial transcript from April 29th, page 145, line 16 to 20?
Q These are question and answer to Mr. Lowett, I believe from me.
Mr. Lowett, if you wanted to know the values listed for these assets on the books of Lehman Brothers on September 12th or 15th or 16th, would it be better to ask someone what they remember, to look at the actual data from the Lehman systems?
The answer, it would seem to be better to look at the

actual data.
Do you recall seeing that?
A I do.
Q When you said you would defer -- let me just show you one more excerpt on --
MR. HUME: If you could bring up the April 27th trial transcript, which is for Mr. McDade's testimony, page 30, lines 22 to page 31, line 3.
Q This is from Mr. Boies. Question, Mr. McDade, if you, as the President of Lehman Brothers, wanted to know what the difference was between the valuation number estimating the value of Lehman assets, and the Friday night Lehman marks, estimating the value of those same assets, am I correct that you would compare the valuation number with the results from the GFS system. Answer, yes.
Do you recall seeing that?
A I do, yes.
Q And you testified that you would defer to what was actually negotiated in terms of what actually happened. Is it your testimony that the most reliable way to know what the Lehman marks are, is to look at deposition testimony or trial testimony from people who were there during that all nighter, in that chaotic time, or to look at the actual data in the GFS system?
A It's my testimony that the data in the GFS system is the

most reliable. When I read the various -- as I was trying to read the record and read the various statements that were being made, it occurred to me that the way to resolve this as a financial economist, is to simply look at what the numbers are, which is always what you like to do in a situation like this.

Q You also were asked some questions earlier today, Professor Pfleiderer, about whether you had ever analyzed whether the short positions on the liability side of that Berkenfeld schedule had been marked up. Do you recall those questions?

A Yes, I do.

Q And I think you testified you hadn't analyzed that.

A That was not something that I had looked into.

Q Do you recall, Professor Pfleiderer, in your review of the Movant's Rule 60 brief, of all of their other papers, all the trial testimony, whether they have ever previously, as far as you know, raised the assertion that what happened, was that the short positions on the trading liabilities were marked up?

A I believe I've read most of their -- well, I should be careful here. I've read quite a few of their filings. I haven't read everything, but I've never seen any allegation or any testimony or anything that relates to marking up the short position, so I certainly have not read anything of that sort.

Q And would it be your understanding that an allegation that the short positions on the right-hand side of the schedule had

been marked up, that would be a very different factual allegation, from an allegation that was actually made that the long positions had been marked down?

A Indeed that would be very different and require a whole different sort of analysis, and so it would be very different.

Q You were also asked some questions about the equities, the valuation of the equities. And first was the issue of the timing of the valuation, and when Barclays actually received the equities. Do you recall those questions?

A Yes, I do.

Q And you were shown slide, demonstrative slide 89 of yours, which refers to when certain batches of inventory were transferred to Barclays. Do you recall that?

A Yes.

Q Is your use of the word transfer in that demonstrative, and generally in your testimony, a technical discussion of when Barclays received full legal ownership and the ability to sell the securities?

A Certainly as a financial economist, in terms of forming my opinions, I was wanting to factor in when I, as an economist, interpreted they had full control. So I know that transfer is used in various ways. For instance, transferring the custodian for various securities from JPMorgan to BoNY, but those type of transfers was not what I had in mind, in any way, in terms of thinking about what the economics of the transaction are and

when Barclays would have basically ownership and be able to sell the assets.
Q Do you understand that there may be a difference between when assets are pledged, which may be referred to it as transferred, for purposes of repo, and when they are fully transferred for all legal purposes in a sale?
A That's my understanding. Again, I'm a layperson, and not an attorney, but I certainly do understand that there is a distinction or should be that distinction.
Q Then you were asked some questions about the bid offer adjustment on the equities. And you were shown, I think, one of your demonstratives that referred to a PwC document describing where their spreads were wider in September. Do you recall that?
A Yes.
Q I think Mr. Tambe said you know that not to be true. Do you recall that?
A Yes, I do.
Q And then there was a reference made to what the comparison is that Mr. -- Professor Zchemiasky did on the simple average of the bid offer adjustments -- bid offer spreads, sorry, that were gathered, that were actually possible to be gathered by Barclays for December versus those in September. Do you recall that?
A Yes.

Q Do you recall that that analysis showed that the simple average of those observable bid-ask spreads show wider spreads in December than in September?

A That is correct.

Q And did you understand that to be what Mr. Tambe was referring to when he said, you know that's not true?

A Yes. I thought he was referring to the 450 million comparison.

MR. HUME: Can I just ask that the hypothetical example shown to Professor Zchemiasky be pulled up briefly on the screen.

Q Professor Pfleiderer, is it mathematically possible that the simple average of bid-ask spreads could be shown to be greater in December than in September, even though for a majority of the CUSIPs, the ratio is, in fact, greater in September than December? Is that mathematically possible?

A Oh, indeed, and this would be one of an infinite number of ways to illustrate that, yes.

Q And I'm not representing to you or asking you to say that this is exactly what the inventory was that Barclays acquired, I'm simply asking you to explain to the Court, is this mathematically possible, and can you explain what's happening here?

A Yes. Basically, what we see here is in September for, I guess it's nine out of ten CUSIPs, the spread is larger, but

for one CUSIP, you see that it's going the other way in a substantial direction. So when you take the average across these, the average is going to be heavily affected by number ten, and that's going to create this difference in the average and yet, we have nine out of ten that are larger in September.

So mathematically, all kinds of things can occur mathematically. And so it's very difficult to make a judgment as to how to cover those question marks that I talked about where you don't have the data.

Q You were also asked questions about the December settlement securities. Do you recall that?

A Yes.

Q And you were first asked a series of questions with the formulation of what exactly the concept of the settlement was, and you were --

A Yes.

Q -- shown an excerpt where the Court gave its understanding of what was happening in the settlement. Do you recall that?

A I do.

MR. HUME: Could we just pull that back up again? It's the December 22nd transcript initially at page 41.

Q And I don't -- I think beginning line 15 to the bottom is what you were shown by Mr. Tambe. And he says -- the Court asks, I would like better clarity that I currently have on a valuation question.

He goes on to say, I believe if I'm understanding the transaction correctly, that the working premise of it, is that the 1.25 billion dollars in cash consideration, which is going to Barclays upon approval, along with the securities that have been identified, is intended to compensate Barclays -- go to the next page -- for the diminution in value over time of those securities. Such as Barclays is receiving the same seven billion dollars in value, assuming it's proved today and consummated tomorrow, they would've received if the transaction would've been consummated as contemplated in September.

Do you see all of that?

A Yes, I do.

Q And do you see that Judge Peck then says, am I right in understanding that.

A Yes.

Q Do you understand that Judge Peck was asking a question?

A Yes, it's clearly a question.

Q Let me show you, if I could, what comes after that question from Mr. Schiller at page 42, lines 9 to 12. Immediately after the question is asked, Mr. Schiller says, it's a bit different than that, Judge. The cash component is designed to address the liquidation of certain securities from the Fed portfolio that occurred, and it makes up for that portion of the securities.

Do you see that?

A   Yes, I do.
Q   So is it your understanding, Professor Pfleiderer, that there was no compensation to Barclays for the diminution in value of the security portion of the December settlement?
A   I'd probably have to read in more context around it, but that certainly implies that the nuances of this are different than what was originally posed. So, yes, I would understand that it is subject to a different interpretation.
Q   Let me, if I could, just pull up Movant's 640, which -- and I'll just tell you in a moment. This is an e-mail from Harold Novikoff at Wachtell Lipton, who was a lawyer for JPMorgan on October 31, 2008.
     And in the second paragraph when he describes the securities on the list, are all the securities financed by the Fed. Do you see that, on the evening of September 17th?
A   Yes, I do.
Q   And the second sentence says, a number of securities financed by the Fed after September 17th, but were not previously delivered to BarCap were liquidated by JPMorgan before this settlement took shape.
     Do you see that?
A   Yes, I do.
Q   And he says -- goes on to say, which is the reason for the need to make a cash payment as part of the settlement. Do you see that?

A Yes, I do.
Q What impact, if any, does that e-mail, that information and Mr. Schiller's statement at the December 22nd hearing have on your analysis and opinion in this case?
A So now I understand the nature of this settlement a little better than I did when I woke up this morning, and it indicates to me that this is sort of ex post settling up based upon the fact that some of those securities were liquidated into cash, and the cash is being delivered.
And again, I would understand this to mean that it is still inappropriate to do what the movants are asking to be done, which is to value this on the 22nd, when in fact, you didn't have control of those securities, and in fact, JPMorgan had control of those securities and was liquidating them at various points in time. So again, based on this understanding, I believe this reinforces my view that it's inappropriate to do what the movants are suggesting.
Q Let me direct your attention, Professor Pfleiderer, to the first paragraph, which says, I've attached the spreadsheet with collateral values in quotes, as of September 17th, which was the last evening on which the Fed provided financing.
Do you see that?
A Yes, I do.
Q The next sentence says, I understand that these collateral values were furnished principally by third party pricing

sources, and we caution against using those values as reliable indicators of realizable value.

Do you see that?

A Yes, I do.

Q What impact, if any, does that have on your analysis or opinion?

A Well, I can read that in two ways, both in the same import. One is that the custodial marks are not basically reliable as it said, I'm basically just repeating it, for calculating what their realizable value was, and also pointing out that you're getting these later, and so the September 17th value is not appropriate.

Q You were also asked questions about statements in your report about the Fed -- the Federal Reserve's insistence that Barclays take its place in the repo lending facility. Do you recall that?

A Yes, I was.

Q And I'd like to just show you one quick excerpt from the trial testimony. You were asked if you would defer to Shari Leventhal. Do you recall that?

A Yes. I was asked if I would, and I said that I certainly would.

Q I'd just like to pull up a brief transcript from the September 7th, 2010 trial testimony at page 8, line 24 to page 9, line 5.

MR. HUME: It must be a different page eight.

UNIDENTIFIED SPEAKER: Sorry.

MR. HUME: Page 8, line 24, beginning of the question. There we go, okay.

Q Question: All right, and there were some -- this looks like the incorrect cite.

MR. HUME: Is this from September 7th, 2010? This is trial testimony from Shari Leventhal from the Fed.

(Pause)

Q Question: And did you require Barclays do an agreement on September 17th to take out the Fed's exposure to LBI.

Do you see that?

A Yes, I do.

Q Answer: Yes, we did. We required Barclays to agree to assume the obligation to finance LBI.

Do you see that?

A I do.

Q And is that consistent with your understanding as stated in your report?

A That was not the basis for my understanding, but it's certainly very consistent with my understanding.

Q You were also asked some questions by Mr. Tambe about the incentives of the Barclays' traders. Do you recall that?

A Yes, I do.

Q And was this testimony about -- there was questions about

whether the traders had an incentive because if they marked the assets down, they could make a profit, which would increase their personal compensation. Do you recall that?
A Yes. I believe that was what was behind the question, I believe.
Q And you were asked whether you had done any investigation into the precise nature of the compensation structure of the traders, as opposed to just having a general understanding. Do you recall that?
A Yes, I do.
Q Do you know one way or the other, Professor Pfleiderer, whether movants have taken detailed discovery to find out what the precise nature of the compensation structure of those traders is? Do you know one way or the other?
A I did not know one way or the other.
Q Since you were asked questions about those incentives, I'd like to ask you another question.
Assuming that traders have some direct or indirect relationship between their compensation and profits on their desks, is it your opinion as a financial economist, do you have an opinion about the incentives of the organization to ensure that those profits are legitimate?
A As a financial economist, I would say and certainly if I were a shareholder at Barclays, I would say that a compensation scheme that allows traders to mark assets down, so that they

can increase their P&L is not a compensation system that I would want to see. And if I were overseeing an institution like Barclays, I certainly would not base compensation on that. And, in fact, my understanding is that that is why you have a product control group or independent price testing, to make sure that that basically is not happening. At least that is one way to make sure that the marks of a front office is putting on assets are not basically misrepresenting what those assets are worth.

And I know this isn't dealing with traders, but I remember very distinctly when I was talking to Gary Romain on the phone in December, there were a series of questions that we were asking and I think I asked one of them, to make sure that his compensation and all those that are involved in this independent price testing was not based on whether the marks were high or low, and he was emphatic in saying that that was not the case.

And so overall, those are the people that are charged with putting the ultimate marks that go onto the acquisition balance sheet.

Q In addition to the incentive structure you just identified, did Barclays, as an organization, and did its senior management, have an incentive or at least a desire, based on your understanding as a financial economist, to have as large a negative goodwill number on their acquisition

balance sheet as possible?

A So there certainly was an incentive for a bank, especially at this time to have larger valuation put on this to increase its registered capital, or its reported capital, given especially at this time. It was difficult potentially to raise capital. There would have been, if any, incentive for the organization as a whole to have this recorded on the balance sheet and not in the P&L later on to give capital immediately.

And I'm not saying that -- and I want to be careful. I'm saying that that would be an incentive. I'm not saying that the organization pushed for marks to be higher for that. I'm not making any accusation of that sort clearly, but there would be an incentive that would go in that direction.

MR. HUME: Could we briefly show an excerpt from the April 30th, 2010 trial transcript, the testimony of Barclay's CFO Patrick Clackson, page 32, line 24 to page 33, line 5?

Q I apologize I don't know who's doing the questioning here, but the question is: What did you do in response to that statement or observation from Mr. Ricci, need to get to four or no write down capacity. Well, if you didn't understand what he meant, you probably didn't know what to do, right?

I think I now think this was a question from Mr. Gaffney.

Answer: Yeah, no, I mean, as I said, we were looking at everything, and yes, we obviously wanted as large a number as possible.

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Do you see that?
A Yes.
Q And does that have any relevance or impact on your analysis and opinion in this case?
A I would interpret this as again being motivated to make sure that their capital was not impaired when this transaction was completed, and the desire that it be what, I guess, some people call capital accretive, so that the bank could post higher capital.
Q You were asked a number of questions, Professor Pfleiderer, by Mr. Tambe throughout the day, about whether you would defer to those who had a feel for the market. Do you recall that?
A Yes, I do.
Q And when you were answering those questions, was it your understanding that you were being asked, whether you deferred to people who are actively trading in the market, and who had a feel for the market at that time, in September 2008?
A That was how I interpreted the question, that basically was the question I was answering, yes.
Q If the question instead was, would you defer to people who had traded not at that time, and who were not active in the market at that time, but instead may have traded at other times, and who were giving an opinion in a litigation context, would your answer have been the same?

A No, absolutely not. A feel for the market was not the feel for a market at some time, it was the feel for this particular market in late September of 2008. So that was how I was answering the question, and I would take someone who had experience at another time not to really have the experience that was needed here.
Q You were asked some questions about how the process of your doing the work in this case, and the role of your staff, in helping to gather information. Do you recall that?
A Yes, I do.
Q Now, when you said you had a number of oral conversations with your staff, do you recall that?
A Yes, quite a few.
Q In those conversations, were you having conversations about documents and spreadsheets that related to the valuation of the assets and that have been produced in this case?
A Many of those discussions were about that, yes.
Q And was it in an effort to understand those documents and spreadsheets as best as possible that you were engaged in that work?
A Yes. Many of the discussions were centered on that issue.
Q You were asked a question or a series of questions about auction-rate securities. Do you recall that?
A Yes, I do.
Q And you were asked about whether it would be reasonable to

value an auction rate security at par, given the nature of the market. Do you recall that?
A Yes, I do.
Q I'd like to pull up BCI Exhibit 1055. This is a document entitled Municipal Auction Rate Securities and Variable Rate Demand Obligations, Interest Rate, and Trading Trends, prepared by the Municipal Securities Rulemaking Board. Do you see that?
A Yes, I do.
Q Are you generally familiar with that body as a standards board in the municipal market?
A Yes, I am.
Q And did you review this document in the course of your work in this case?
A Yes, I did see this.
Q It's a recent document from September 2010. Do you see that?
A Yes.
Q I'd like to refer you to page three of this document.
MR. HUME: And the chart, if we could blow up this chart on the top left of the page.
Q This says municipal ARS trading volume, January '08 to May 2010. Do you see that?
A Yes, I do.
Q And so September 2008 is going to be somewhere in here, correct?

A Yes, somewhere, right about there.
Q Does the information on this chart -- have you reviewed the information on this chart before?
A Yes, I have.
Q Does it have any relevance or impact on your analysis and opinions in this case?
A This actually graphically shows what I was talking about when I mentioned that this market had basically collapsed, or I guess nearly collapsed in February of 2008. And you can see the -- one aspect of that is the trading volume has fallen off by many orders of magnitude here.

MR. HUME: Your Honor, we move BCI Exhibit 1055 into evidence.

MR. TAMBE: Your Honor, it's a hearsay document that can come in for notice or reliance materials by an expert, but it's hearsay.

THE COURT: I don't think it is. It's a -- I'd like to see the cover so I can identify it.

MR. HUME: Can we go back to the cover, please?

THE COURT: This is a document that either is hearsay, subject to an exception where it is the kind of document that is typically relied upon by people in the industry, and has a very high degree of reliability as a means to demonstrate what was going on generally in the market. I have no idea what else in this document. I'm simply looking at it for demonstrative

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purposes. I'm not accepting it as the truth that that is, in fact, the way graphing of the market in auction rate securities at the various times shown on the chart, but I do believe that it is a fair representation of the overall trends, and indeed, the title of the document is trading trends.

To that extent, I believe that it fairly reflects a collapse of that market, and I'm going to admit it.

THE COURT: It's admitted.

(BCI Exhibit 1055, Municipal Securities Rulemaking Board Chart, was hereby received into evidence as of this date.)

MR. HUME: Thank you, Your Honor.

Could you also briefly show BCI Exhibit 1056A?

BY MR. HUME:

Q This is a news article from a publication called Financial Week from June of 2008.

MR. HUME: Would you highlight that so I can make sure I have the date correct? Okay.

Q And on the title of the document is again "Companies Split on Taking ARS Cash Debt", and it reports of 242 firms with disclosed auction rate holdings, fewer than half have owned up to their losses. Do you see that?

A Yes, I do.

Q And do you recall reviewing this article in your preparations and work on this case?

A Yes, I saw it a few weeks ago, if not before.

Q Could we look at the attachment to this article, which I think should be the third or fourth page? Or I think it's embedded in the second page -- I hope we can blow it up, so it's possible to see.

You see we have a -- probably have seen in another article, Look Who's Being Kicked in the ARS. Do you see that?

A Yes, I do.

Q And then it lists a series of companies. Do you see that?

A I do.

Q And it lists a par value for their auction rate securities. Do you see that?

A Yes.

Q And then it lists the fair value and an impairment, and the discount which must be the percentage that the impairment has either to the fair value or the par value, I'm not sure. I assume to the par value.

A It would be to the par value, I believe.

Q Yeah. The fair value is the par value minus the dollar value of the impairment.

A That is correct. I believe that would be what they would be calculating.

Q And what significance, if any, does this have to your analysis in the opinions in this case?

A Well, you can see that a number of the companies are recognizing these losses on their books, are taking substantial

write-downs of these. In many cases, much more than the twenty percent that Barclays took on its ARS portfolio. So you see in the extreme some discounts of seventy-three, sixty-seven percent, some of them are much less, some down below only seven or five percent. I don’t know what you’d get if you would take an average there, but an average, I’m sure, would be on the order of twenty percent if not more, just looking at it and eyeballing it, which I realize is not a terribly reliable way to do it, but you can see there’s just some very substantial discounts there.

MR. HUME: Your Honor, we move BCI Exhibit 1056A into evidence for the limited purpose of showing what was reported at the time about the auction rate securities market, and the write-down being taken.

MR. TAMBE: For that limited purpose, we have no objection.

THE COURT: It’s admitted then for that limited purpose.

THE COURT: It's admitted.

(BCI Exhibit 106A, Financial Week News Article, was hereby received into evidence as of this date.)

BY MR. HUME:

Q Now, Professor Pfleiderer, you were asked also some questions about the work you and your staff did to look for some of these missing mid values in Mark Slattery’s back-up

papers. Do you recall that?
A Yes, I do.
Q And you were asked whether you had reviewed any Barclays' papers as carefully as that.
A Correct.
Q Do you remember generally those questions?
A Yes, I do.
Q Now, did you give testimony yesterday that there were over three hundred mid values in Mr. Slattery's summary work paper, including all of the mid values for the agency RMBS that could not be found in any other work paper?
A No. I don't believe I said all. I said there was a substantial number for which looking through the work papers, there was no calculation apparent of the mid values. All of the models were apparently producing bid marks that were being grossed up.
Q In response to the testimony you gave and the findings that you reported from your staff, did Mr. Tambe show you today any single mid value shown on Mr. Slattery's summary work paper --
A No, I don't believe he did.
Q -- or that they calculated?
A I don't believe he did, no.
Q Did you testify yesterday that if, in fact, Mr. Slattery's model calculated a bid value, what he lists as a bid value, and

then he grossed up to a mid value, and then changed his spreadsheet to show that he was reducing from that mid value to a bid value, that that would be misleading?

A I believe I said something to that effect. I was cautious in the way I said it, but I would take that on face value to be misleading, yes.

Q And in response to that, did Mr. Tambe show you that, in fact, there are work papers showing how any of those mid values were calculated?

A He did not to date, no.

Q Did you see anything in your work -- you did testify about seven or eight bonds, where Barclays had adopted the BoNY marks of .001 and acknowledged that as an oversight. Do you remember that?

A Yes.

Q Did you see -- do you believe Barclays was attempting to be misleading with respect to those bonds?

A No. I certainly believe that that was an oversight.

Q Did you see any evidence in any of your review of any of the work papers, PwC papers, or any of the other work done in this case by Barclays for what they had done, would be considered misleading?

A No, I did not.

Q You were asked a question about how the 47.4 billion dollar number was formulated, and whether it included a

quote/unquote liquidation value. Do you recall that?
A Yes, I do.
Q Now, when Mr. Tambe asked you that, did he define for you precisely what he meant by the phrase liquidation value?
A I am trusting my memory here. I don't believe he did, he may have, but as I recall, I don't believe he did.
Q Do you, as a financial economist, believe the phrase liquidation value can be meant and understood in different ways?
A Indeed, yes.
Q What are those different ways?
A Well, I've seen the term used by traders to simply mean what you sell it for. And so that would be, just again, the exit price that you would get, and then of course, we have liquidation value used perhaps in the context of a Chapter 7 bankruptcy, where you're liquidating something in a situation that's quite different than what you're selling a security in active markets.
So you do need to be careful, and I probably should've been careful interpreting what Mr. Tambe was saying, because liquidation can mean various things in various contexts.
Q Based on your analysis of the assets transferred to Barclays in this transaction, do you believe that in a fire sale liquidation that would've occurred, had there been no sale transaction at all, that the assets transferred -- that the

particular CUSIPs transferred to Barclays in the trading inventory, would have generated as much as 47.4 billion dollars?

A I think it's almost inconceivable that they could've. I think that there would have been a substantial liquidation discount if you're selling those CUSIPs in a very different environment, where the transaction didn't go through.

I can't quantify what that would be, but I can say with great confidence that it would've been significantly less.

Q You were also asked a series of questions at the beginning of the day about whether you knew, whether the lawyers and the Court involved lawyers presenting the sale to the Court and the Court itself was told that there was uncertainty over the asset values, because so many of them were illiquid, and could potentially be valued in different ways. Do you recall that?

A Yes, I do.

Q I'd like to show you, if I could, BCI Exhibit 11, which is the motion filed by Weil Gotshal, lawyers for the debtor, to ask for approval of the sale, and direct your attention to paragraph 17.

Paragraph 17 in the third sentence states, the proposed sale is unique because of the fragile and highly vulnerable nature of the purchased assets. Do you see that?

A Yes, I do.

Q Is that relevant to your opinion in this case?

A That would indicate some of the uncertainties involved in these assets.

Q I ask you now to pull up the September 19th transcript, trial -- sale hearing transcript, September 19th, 2008, at page 109, lines 21 to 22.

This is an answer and when Mark McDade was cross-examined during the sale hearing --

MR. HUME: I think we probably ought to show the question. Sorry about that.

Q Does Lehman have any valuations, internal valuations, of any of the assets that are being transferred to Barclays?

Answer: Absolutely. There are many complex securities involved, many different models that we use to evaluate those securities.

Do you see that?

A Yes, I do.

Q I'd now like to refer you to April 28th trial transcript, page 94, lines 23 to page 95, lines 11. This is the trial testimony of Harvey Miller, who was the lead lawyer for the debtor.

Question: Through that tumultuous week of September 15th through the 22nd, which you've described dramatically this morning again, you never had what you would call an accurate Lehman balance sheet; is that correct?

Answer: That's a fair statement.

Question: And because there was no accurate Lehman balance sheet in that chaotic period, there was significant uncertainty over the value of Lehman's assets and liabilities that were being transferred.

Answer: There was volatility in the values. There was a high level of risk in the transaction, I think particularly from Barclays' perspective, and that was one of the major elements in this volatility, about those transactions during the week, and concern about the decline in the values.

Do you see that?

A Yes, I do.

Q And considering those together with what Lori Fife said at the sale hearing, which you commented upon earlier, do those statements have any relevance or impact on your opinions in this case?

A Yes. Again, I think that they're all supportive of the notion that there was considerable uncertainty during this week, and the nature of these assets, especially given that they're level two and level three assets. So it makes it very difficult to value them, especially when the circumstances in the market are changing so dramatically.

MR. HUME: One minute, Your Honor.

(Pause)

MR. HUME: No further questions, Your Honor. Thank you, Professor Pfleiderer.

THE COURT: Do you have any further cross-examination?

MR. TAMBE: Just one moment, Your Honor.

No further questions, Your Honor. Thank you, Professor Pfleiderer. Thank you.

THE COURT: Professor Pfleiderer, thank you very much.

THE WITNESS: Thank you very much.

THE COURT: You're excused.

Now, I have -- we can get down from the witness stand.

I just have a couple of questions for counsel. During yesterday's examination, there was an attempt to offer BCI Exhibit 1005, which I deferred, in respect to the hearsay objection, concerning particularly the attached spreadsheet. There was an argument as to whether or not it was or wasn't a business record. I'm just wondering what the status is of the Barclays' effort to offer that into evidence, whether there's been any reconciliation of positions with the movants concerning admissibility?

MR. TAMBE: To my knowledge, we haven't had a chance to discuss it.

MR. HUME: We haven't had a chance, Your Honor, but we will discuss it.

THE COURT: But you will discuss that?

MR. HUME: Yes, Your Honor.

THE COURT: Also, I'm not doing this because Mr. Hume has a pattern of sometimes forgetting to offer exhibits, but I

just want to be sure that all exhibits have been offered that you intend to offer in connection with Professor Pfleiderer's testimony. If the answer is no that's fine, if you don't want to proceed with anything.

MR. HUME: The answer is no, I was reminded just as I sat down, that as with the movants, we will want to offer in the demonstratives from Professor Pfleiderer as evidence, and it gives me an opportunity to inform the Court of something we informed movants last night, that one of the demonstratives had a clerical error -- and so we've replaced that, and we'll -- it's slide 71.

THE COURT: Was that the September 2010 versus September 2008 mistake or is there another one?

MR. HUME: No, that's true, actually. There was another -- there was at least one other typo that Professor Pfleiderer recalled during the examination, but this one was this, it was just a pure -- there were two demonstratives for the municipal securities, analyzing them in different way; one, level one, two, three, and one according to auction rate and non-auction rate. And it was that those -- that one of those needed to be corrected was the problem.

THE COURT: I'm not going to know the difference. I mean, they've already served their purpose, but if you wish to make the correction and there's no objection from the movants, that's fine.

MR. TAMBE: No objection to the correction and no objection for this exhibit to come in as a demonstrative exhibit, Your Honor.

THE COURT: Okay. So the demonstratives are admitted with the same limitations that apply to the demonstratives that were admitted in connection with the movant’s expert case.

THE COURT: It's admitted.

(BCI Exhibit, Professor Pfleiderer's Demonstratives, were hereby received into evidence as of this date.)

MR. HUME: Thank you, Your Honor. And in terms of other exhibits, I think our understanding is tomorrow we’re going to be addressing PwC documents. There were some other documents I tried to move in that were reserved objections on, and there are some other exhibits that we’re trying to resolve, we’re going to narrow down, but may need to raise with the Court tomorrow.

THE COURT: Okay. To the extent that the parties are able to reconcile the differences without having to go through an argument on each one, that’s fine. I recognize that the PwC documents are in a separate category and we have the lawyer briefs on that which will help inform the discussion tomorrow, and I’ll see you tomorrow at 10:00 a.m. Thank you.

(Whereupon, the proceedings were recessed at 4:08 p.m., October 7, 2010.)

* * * * *

I N D E X

T E S T I M O N Y

WITNESS	EXAM BY	PAGE	LINE
PAUL PFLEIDERER	MR. TAMBE	5	9
	MR. HUME	156	5

E X H I B I T S

PARTY	NO	DESCRIPTION	ID.	EVID.
BCI	1055	Municipal Securities Rulemaking Board Chart	181	181
BCI	1056A	Financial Week News Article	183	183
BCI		Prof. Pfleiderer’s Demonstratives	192	192

C E R T I F I C A T I O N

I, Ellen Kolman, certify that the foregoing transcript is a true and accurate record of the proceedings.

Ellen S. Kolman

Digitally signed by Ellen S. Kolman
DN: cn=Ellen S. Kolman, c=US
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